

The University of Chicago

# ANTI-CHAIN-STORE TAX LEGISLATION

A PART OF A DISSERTATION SUBMITTED  
TO THE FACULTY OF THE SCHOOL  
OF BUSINESS IN CANDIDACY FOR THE  
DEGREE OF DOCTOR OF PHILOSOPHY

1939

By  
MAURICE W. LEE

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## PREFACE

THIS material has been prepared as a study in one phase of government control of business. Only one chapter may be said to deal directly with the nature of retail distribution. The remaining chapters are concerned with problems of control, the philosophy of control, and specific techniques of regulation. While the major interest lies with the effect of state discriminatory taxes upon corporate chain stores, the analysis would have been incomplete without some consideration of other types of regulatory legislation which have recently appeared. One entire chapter has, in fact, been devoted to such measures as the federal Robinson-Patman Act, the Miller-Tydings Act, and state fair-trade-practice laws.

This study is heavily indebted, as all which analyze the corporate chains must be, to the Federal Trade Commission for clarification of innumerable points on chain-store operation. The Commission survey, covering thirty-three volumes, constitutes the most intensive analysis available in this field.

The writer is indebted to Professors Cox and Palmer, who read the manuscript during its early stages, and to Professors Nerlove and Duddy, whose suggestions throughout the entire study have been most helpful. The greatest measure of gratitude must go to Dean William H. Spencer of the School of Business of the University of Chicago. The study was initiated at his suggestion, carried on under his guidance, and owes much to his many suggestions.

M. W. L.



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## CHAPTER I

### INTRODUCTION

WHILE the relationship between government and industry has become more complex, some clarification is being found through analysis of particular instances of politico-business affinity. This study of certain of the relationships is offered as a type case. Emphasis is placed upon state discriminatory chain-store taxes. One of the principal reasons for so limiting the scope of the study lies in the fact that historically most chain-control bills have been taxing statutes designed to impair the competitive advantage of the corporate chain retailers.

Other statutes aimed at chain-store practices have already received a considerable amount of attention. The Robinson-Patman Act has been the subject of an avalanche of criticism, explanation, and analysis. The Miller-Tydings bill of the federal government and the state fair-trade-practice statutes have likewise achieved a not inconsiderable measure of publicity. For these reasons there appears to be little excuse for including any extended discussion of these laws.

Chain-store taxation can be evaluated only in so far as its locus in the whole field of regulation is perceived. The need for such taxes, or the lack thereof, can be realized only when the measure of control exerted by other statutes is also understood. The discussion of the Robinson-Patman and Miller-Tydings acts and of the state fair-trade-practice statutes is therefore to be considered only in its relation to the main line of study, the state taxation of the corporate chain stores.

#### BACKGROUND OF CHAIN-STORE CONTROL

Discussion of the relation which might properly be thought to exist between government and business formerly revolved around the right of government to exercise anything more than a nominal amount of control. Now the controversy has advanced to the

point where the issue lies in the choice of methods of regulation to be used.

Railroads and public utilities were among the first groups placed under government supervision. At a slightly later date legislation was designed to check practices of groups which were neither carriers nor utilities. Most of this legislation, however, was general in nature, directed at business practices and policies but not at specific entities or selected industries.

More recently there has been a change. Broad, sweeping patterns of control are being replaced by custom-made laws designed to fit the conditions in particular fields. The regulation of the petroleum, bituminous-coal, and radio-broadcasting industries is illustrative. In these cases, however, the industries themselves were not unwilling to admit the failure of private control—were even anxious that some type of government regulation be introduced. Here, then, is found a new phase in the cycle of regulation, a stage in which legislation adapted to specific industries is applied.

The case of the chain stores is somewhat different. Whereas the industries cited above were openly seeking outside regulation, the chains were insistent that no external control was needed. The legislation which was introduced to cover the corporate chains was similar to that cited above as governing the petroleum, radio, and bituminous coal fields only in the sense that it also was custom built to fit the regulated entity. It differed inasmuch as the chains did not want outside regulation, saw little need for it, and felt that competition was sufficiently effective for purposes of maintaining order in the distributive field.

#### HYPOTHESES

The hypotheses upon which the following thesis may be said to rest can be expressed as follows:

1. Competition where effective is preferable to regulation.
2. Regulation, because it constitutes a departure from previous custom, should be kept at a minimum, lest the disturbance which it produces may bring about losses far in excess of those inherent in the practices and customs of the group to be regulated.

3. The corporate chains have, historically, introduced many revisions in merchandising technique, and in general the public has experienced appreciable benefit from these revisions.

4. Great care must be taken in regulating such groups lest the beneficial aspects be destroyed with no compensating public gains.

5. In judging the merits of a regulatory program the impact upon the regulated body should be given little consideration when compared with the necessity of studying the effect upon general welfare.

#### METHODOLOGY

The manner of approach to the study is relatively simple. It involves only the presentation, analysis, and evaluation of the anti-chain-taxing laws.

A detailed study of only the leading statutes is required. Of the more than fifty state laws which impose discriminatory chain taxes only some fifteen are presented in detail and of these only three or four are intensively scanned.

The evaluation of the statutes follows two broad lines of inquiry. The first has to do with the legalistic nature of the measures and involves the issue of constitutionality. The second deals with the economic effect of the taxes; with their impact upon costs and upon profit margins; with the incidence of the taxes; and, finally, with their regulatory effects.

#### PURPOSES OF THE STUDY

This study is not intended to be an analysis of marketing problems. It is being offered as a contribution in the rapidly expanding field of government and business. Its value lies in whatever light it may throw upon one instance of government regulation, the state programs of discriminatory chain-store taxation.

Some contribution has been made, the writer feels, in the collection and classification of the many statutes. A like contribution may be discovered in the collection of court decisions governing the development of this control legislation.

Of more importance than these somewhat mechanical aspects

is the evaluation offered. The study was made for the purpose of determining the desirability of such legislation. Consequently the major contribution lies in the conclusion reached on this point and the methods by which that conclusion was attained. The section dealing with the incidence of chain-store taxes is of value in this connection.

## CHAPTER II

### THE DEVELOPMENT OF ANTI-CHAIN TAXES

THE early 1920's witnessed the development of a reaction against the corporate chains which grew increasingly hostile. This attitude originated in the ranks of the independent retailers and wholesalers, but for some considerable period of time was not evident in the public mind.<sup>1</sup> Groups of independent businessmen, representing a militant minority, were able to impress legislators with the political value of their cause. It is, in reality, a mistake in terminology to call this early anti-chain movement a social-control program. It was instigated by any but social motives. Its sponsors were a group more interested in penalizing their rivals than in considering whether such penalization might have a beneficial or detrimental effect upon the public. The significant point, however, is the fact that in the middle 1920's a movement began to control and curb the expanding power of the corporate chain.

In 1925 the first legislative crystallization of such feeling occurred when two states considered the enactment of bills to check the chain stores. Neither of these proposals was enacted. In 1926 one such bill was introduced, but again the required support was not in evidence and it was not until the next year that anti-chain statutes actually made their appearance in the code books of the various states.<sup>2</sup>

In 1927 Georgia, Maryland, and North Carolina enacted anti-chain bills and from that date until the present the movement has

<sup>1</sup> The writer has been unable to find any body of references to the antisocial nature of the chain stores until the 1920's were well under way. Textbooks and popular articles which touched on these groups nearly all joined in praising the efficiency and low-cost operations enjoyed by these rapidly growing systems of distribution.

<sup>2</sup> Charles F. Phillips, "State Discriminatory Chain Store Taxation," *Harvard Business Review*, XIV (1935), 348.



continued with little interruption. At the end of 1938 such measures were in force in twenty-four of the states.

The bitter attitude of the small independent retailer was beginning to make itself felt in the legislatures of certain of the states by the middle of the decade. As indicated above, the first of these punitive bills taxing the chains was introduced in 1925.<sup>3</sup> There are no prior bills on record and both of the foregoing bills failed to come through the legislatures. In the following year, an off-legislative one, only a single bill was introduced, and this likewise failed of enactment.

The year 1927, in which most of the legislatures held session, was an important one for the chains. Under increasing pressure from the small retailers fifteen states considered such statutes and for the first time in the history of the country laws discriminating directly against the chain systems of distribution were placed on state statute books. This occurred in Georgia, Maryland, and North Carolina. All three of these acts were ultimately declared unconstitutional. The movement had begun, however, and in 1928, an off-legislative year, five states considered such proposals and two enacted formal statutes (South Carolina and Virginia). The South Carolina law, like its predecessors, was declared unconstitutional. The Virginia law was more fortunate and remained on the code books of that state until replaced by another act at a later date.

The year 1929 was one in which the majority of the states held legislative assemblies and 62 of these bills were considered, with 4 finally passing. Of the 4, 2 were enacted to replace earlier statutes which had been declared unconstitutional. These were the bills of North Carolina and Georgia. The two newcomers were New Hampshire and Indiana. In 1930, 80 bills were proposed and 3 enacted. One of these was a replacement for an earlier law to which the courts had taken exception, South Carolina. The other 2 came from Mississippi and Kentucky.

In 1931, 126 such bills were considered and 5 were passed. In 1932, 125 were up for discussion and 3 were accepted, in widely

<sup>3</sup> *Ibid.*

scattered parts of the country—Arizona, Louisiana, and Wisconsin. The movement was gaining momentum and spreading rapidly.

In the following year, 1933, during which most of the legislative groups were in session, a record number of bills was considered, 225. The number passed also exceeded all previous records. In all, 13 such measures made their way into the statute books before the end of the year, and they came from all sections of the nation. In the South, Florida joined the ranks of those who had already passed discriminatory legislation against the chains. On the Atlantic seaboard Maryland and North Carolina joined the ranks with new statutes. In the Middle West, Indiana, Michigan, Wisconsin, West Virginia, and Minnesota passed such bills—the Indiana law increasing the rates of the original levy passed in 1929. The West was represented by Idaho, Montana, and New Mexico, while New England added Vermont and Maine to complete the list of thirteen. In 1934, which was an off-legislative year, only four states enacted such bills. One of these was a newcomer, Colorado, while Kentucky, Virginia, and New Mexico modified their existing acts or replaced them with different measures.

In 1935 seven states contributed to the rapidly increasing list. Iowa, South Dakota, and California were new arrivals; Florida and North Carolina revised already existent bills; Nebraska and Virginia passed statutes which were relatively weak and non-discriminatory, although aimed at the chain stores. A total of 152 bills had been proposed during the course of the year. The year 1936 saw the movement losing some of its momentum, although 31 bills were proposed and 2 were passed. By January 1, 1937, there were anti-chain acts in operation in twenty states. One year later there were 24 such bills in force, 2 of which—those of Virginia and Delaware—were relatively unimportant.

The year 1938 became the first in which no new taxing statutes were passed since the first measures entered the books in 1928. Two factors explain this. In the first place, 1938 was an off-legis-

lative year; in the second, the chains were beginning to bring pressure to bear in order to prevent the passage of such bills.<sup>4</sup> In New York, Arkansas, and Mississippi new or revising measures failed of enactment. In South Carolina the legislature adjourned without enacting any of three proposals to increase rates now current under the existing statute. Bills proposed in Ohio and New Jersey were referred to committee and have not appeared. An anti-chain-store agitator in Oklahoma has taken out a petition to have such a bill introduced, but at last report was experiencing difficulty in obtaining the necessary 90,000 signatures.<sup>5</sup> On January 1, 1939, there had been no change over the position one year earlier. Twenty-four states had punitive chain legislation of varying degrees of severity.

The passage of the Pennsylvania statute on June 5, 1937, marked an important date in the evolution of chain taxing laws, inasmuch as it introduced the movement in the larger industrial states. Prior to that date the chain advocates had felt that there was little likelihood of such legislation arising in the financial and industrial centers, where it was believed sentiment favored the chains strongly. With the signing of this statute the remaining industrial states showed increased interest in the possibilities of such legislation. Illinois, New York, New Jersey, Ohio, and Massachusetts have all seen such bills introduced for serious consideration.

Other states which entered the taxing group with new or revised measures in 1937 were Wisconsin, Montana, North Carolina, South Dakota, Tennessee, Georgia, and Minnesota. The Wisconsin act was passed to replace one which had previously expired. The Montana law replaced the 1933 statute, which had been repealed. North Carolina, one of the original three of 1927, enacted a new bill, its fourth since that date. The 1937 enactment was nearly a replica of the 1935 bill. The South Dakota bill replaced the emergency measure of 1935, which had been declared

<sup>4</sup> Inigo Brown, "Chains Prepare for Battle in the Eleventh Hour," *Chain Store Review: Groceries*, September, 1938, pp. 3-4, presents a discussion of the activities of the chains in open opposition to these proposals.

<sup>5</sup> *Chain Store Age*, June, 1936, p. 66.

unconstitutional in 1936. The Tennessee enactment was a unique affair of which more will be said later. The Georgia bill imposed a levy upon mail-order houses as well as general chains and thereby established something of a precedent. Minnesota's statute was passed to replace its 1935 measure, declared unconstitutional in

TABLE 1\*  
SUMMARY DATA ON STATE CHAIN TAXING BILLS

| State                | Date of Enactment | Minimum Stores Applicable | Minimum Tax | Maximum Stores | Maximum Tax |
|----------------------|-------------------|---------------------------|-------------|----------------|-------------|
| Alabama .....        | 1935              | 1                         | \$ 1.00     | 21             | \$112.50    |
| Colorado .....       | 1935              | 1                         | 2.00        | 25             | 300.00      |
| Florida .....        | 1935              | 1                         | 10.00       | 16             | 400.00      |
| Georgia .....        | 1936              | 1                         | 2.00        | 41             | 200.00      |
| Idaho .....          | 1933              | 1                         | 5.00        | 20             | 500.00      |
| Indiana .....        | 1933              | 1                         | 3.00        | 21             | 150.00      |
| Iowa .....           | 1935              | 2                         | 5.00        | 51             | 155.00      |
| Kentucky .....       | 1934              | 1                         | 2.00        | 51             | 150.00      |
| Louisiana .....      | 1934              | 1                         | 10.00       | 501            | 550.00      |
| Maryland .....       | 1933              | 2                         | 5.00        | 21             | 150.00      |
| Michigan .....       | 1935              | 2                         | 10.00       | 26             | 250.00      |
| Minnesota .....      | 1937              | 1                         | 10.00       | 151            | 350.00      |
| Mississippi .....    | 1936              | 2                         | 3.00        | 41             | 300.00      |
| Montana .....        | 1937              | 1                         | 5.00        | 5              | 200.00      |
| North Carolina ..... | 1937              | 2                         | 50.00       | 201            | 225.00      |
| Pennsylvania .....   | 1937              | 1                         | 1.00        | 501            | 500.00      |
| South Carolina ..... | 1930              | 1                         | 5.00        | 30             | 150.00      |
| South Dakota .....   | 1937              | 1                         | 1.00        | 41             | 250.00      |
| Texas .....          | 1935              | 1                         | 1.00        | 51             | 750.00      |
| West Virginia .....  | 1933              | 1                         | 2.00        | 76             | 250.00      |
| Wisconsin .....      | 1937              | 2                         | 25.00       | 26             | 100.00      |
| Average .....        |                   | 1.28                      | \$ 7.52     | 91.24          | \$285.36    |

\*Delaware, Virginia, and Tennessee excluded, either as nondiscriminatory or because based upon different principle than the foregoing. Years refer to date of passage.

Source: code books, statute books, and copies of chain-store taxing bills of the various states.

1937 by a state court, and, like the Georgia bill, it imposed a special tax on mail-order-chain outlets.

The twenty-four state laws discriminating against the chains were distributed throughout nearly all sections of the country, as illustrated in Table 1. They were to be found in Alabama, Colorado, Delaware, Florida, Georgia, Iowa, Indiana, Idaho, Maryland, Michigan, Minnesota, Mississippi, Louisiana, Kentucky, Montana, North Carolina, Pennsylvania, South Carolina, South



Dakota, Tennessee, Texas, Virginia, West Virginia, and Wisconsin. Of these the Virginia and Delaware laws could scarcely be classified as discriminating solely against the chain stores, although they are usually included in this class.

The third column in the table indicates the point at which the tax is first levied, in some states on the first store of a chain and in others only after the first has been excluded. For all states combined the taxes are first imposed on the 1.285th store. The fourth column refers to the amount of tax at the first level—i.e., before progression. This, it is found, ranges from a low of \$1.00 to a high of \$50.00, with an average tax of \$7.52 imposed on the 1.285th store (see above). The next column indicates the point at which progression stops; for all stores beyond that level the tax is uniform at the highest rate. The state bills tend, on the average, to stop progressing at the 91.24th store. The final column indicates the tax rate at the maximum point, and is found to average, for all states, \$285.36 for the 91st store and all thereafter.

This completes the chronological story of state chain-store taxation to January 1, 1939. The movement has by no means come to an end, notwithstanding the fact that no such proposals were adopted during 1938. The chains themselves are greatly concerned as to the future.

#### NATURE OF THE ANTI-CHAIN TAXES

The earlier taxing laws dropped smoothly into one of two classifications. They imposed rates which graduated to higher levels either as the number of stores in the chain increased, or as the volume of gross sales of the chain rose. Later enactments destroyed the simplicity of this arrangement and today there are at least nine bases for classification, most of them being modifications of the original method, with rates graduated as the number of stores under single control increases. Table 2 represents an attempt to present this classification in such fashion as will include all of the various patterns adopted by the legislators since the inception of the movement.

The first of the statutes in Table 2 established an outright refusal to permit the existence of chains having more than a pre-



scribed number of stores under single management. It may be noted that such a law appeared in only a single state. It was an act of the state of Maryland and, being passed in 1927, was the first of the anti-chain statutes. A heated controversy immediately brought the bill into the state courts, where it was declared unconstitutional, and the opinion of the court was so emphatic con-

TABLE 2\*  
TABULATION OF DISCRIMINATORY ANTI-CHAIN LEGISLATION  
OF THE STATE GOVERNMENTS

| Nature of Statute                                                                  | Illustrative State Law | Court Ruling     |
|------------------------------------------------------------------------------------|------------------------|------------------|
| 1. Outright prohibition. . . . .                                                   | Maryland, 1927         | Unconstitutional |
| 2. Flat tax on chains of more than exempted number of stores. . . . .              | North Carolina, 1927   | Unconstitutional |
| 3. Tax graduated as number of stores in chain increases. . . . .                   | Indiana, 1928          | Constitutional   |
| 4. Tax graduated as volume of gross sales by chain increases. . . . .              | Kentucky, 1939         | Unconstitutional |
| 5. Combination of Types 3 and 4. . . . .                                           | Minnesota, 1933        | Unconstitutional |
| 6. Like Type 3 but number of stores considered as number wherever located. . . . . | Louisiana, 1934        | Constitutional   |
| 7. Like Type 3 but imposed on chain and chain counters. . . . .                    | Michigan, 1935         | Constitutional   |
| 8. Like Type 3, imposed on mail-order chains as well as others. . . . .            | Georgia, 1936          | ?†               |
| 9. Tax based on amount of floor space occupied by all stores of chain. . . . .     | Tennessee, 1936        | ?‡               |

\* Source: code books, statute books, and chain-taxing laws of the various states.

† While this law has not been fully settled in the courts there seems little doubt of its constitutionality.

‡ There are no indications that the chains are making any effort to have this law set aside. At the present time they may be quite content to reside under its rather moderate penalties, rather than contest the law and if successful run the risk of having it replaced by one much more punitive.

cerning the arbitrary nature of the statute that no other state has ventured to duplicate its form. This bill, accordingly, is of no more than historical significance in the present discussion.

North Carolina in 1927 enacted a statute which was something of a variant of the foregoing. This act permitted the existence of a minimum number of stores under single management and exempted that number from taxation, but imposed a fee on each store of a chain of greater number. The statute set a flat assessment on every store of a chain having more than five stores. The rate was \$50 for each outlet. Any chain having five or less units

was excused from payment of the tax, but a chain of six or more stores was compelled to pay a \$50 tax on each store, including the first five.<sup>6</sup> After this law was declared unconstitutional the state of North Carolina modified it by another act in 1929, which made the tax of the former act applicable to all stores over one.<sup>7</sup> In this fashion a tax was levied upon all chain groups, but the independent dealers were fully excused from any payment under the terms of that act.

The third type of statute is, by all odds, the most popular of the chain-store taxing bills. There is a great amount of variance in the tax rates imposed under the different acts in this group, but in other respects they all conform to a rough pattern of similarity. The majority set taxes at a low rate on a single store or exempt the first entirely, then increase the rates progressively as the number of stores in a given chain increases. A representative tax is that levied by Indiana in 1933.<sup>8</sup> Here a tax of \$3.00 is imposed on the first store, a tax of \$10 on the second to fifth inclusive, \$20 on the sixth to tenth, \$30 on the eleventh to twentieth, and a tax of \$150 on all stores over twenty. A chain in Indiana, having twenty-five stores, all located within the state, would compute its tax bill as follows:

|                                                     |                |
|-----------------------------------------------------|----------------|
| For the first store . . . . .                       | \$ 3           |
| For the second to fifth (\$10 each) . . . . .       | 40             |
| For the sixth to tenth (\$20 each) . . . . .        | 100            |
| For the eleventh to twentieth (\$30 each) . . . . . | 300            |
| For all over twenty (\$150 each) . . . . .          | 750            |
| Total tax bill . . . . .                            | <u>\$1,193</u> |

Thus a chain of twenty-five stores would pay an annual sum of \$1,193 for the privilege of operating in chain form in Indiana. This would amount to an average yearly assessment of \$47.72 per store. Such an imposition would not, in all likelihood, impair the future of the average chain system, but that aspect of the problem will be discussed in a later chapter.

The original Indiana act, similar to this but imposing lower

<sup>6</sup> *Laws of North Carolina*, 1927, c. 80, sec. 162.

<sup>7</sup> *Ibid.*, 1929, c. 345, sec. 162.

<sup>8</sup> *Laws of Indiana*, 1933, c. 271.

rates of taxation, is interesting chiefly because it was the first of the chain taxing statutes to receive the official sanction of the United States Supreme Court. The 1928 act, like the 1933 bill, imposed its highest rates on those stores in excess of twenty. This difference existed, however: whereas the highest rate under the 1928 act was only \$25 per store, under the 1933 measure it amounted to six times that figure, \$150.<sup>9</sup>

Of the twenty-nine states which have at one time or another imposed these statutes, the majority have at some period adopted a form of enactment corresponding to the pattern of this third group.

Florida imposes one of the highest taxes, a levy of \$400 being placed on every store over sixteen.<sup>10</sup> The California act of 1935, which never became effective due to injunctive restraint, proposed rates as high as \$500 for each store in excess of ten,<sup>11</sup> and the Idaho law of 1933 reached a similar figure for all stores in excess of nineteen.<sup>12</sup> Pennsylvania's maximum rate of \$500 did not apply until more than five hundred stores had been reached.<sup>13</sup> The Texas law of 1935 levied a tax which established the top level for these bills, a figure of \$750 on every store in excess of fifty.<sup>14</sup> This law was held in abeyance until court action could determine its validity, but finally went into operation after a favorable decision had been rendered by the Texas Supreme Court on December 1, 1937. Mississippi's 1936 law reached a peak at \$300 on the forty-first store and all thereafter,<sup>15</sup> and the Colorado law of 1935 reached a similar levy at the twenty-fifth store.<sup>16</sup>

On the other side of the picture there were several states whose laws imposed only a nominal tax upon the chains. Maine in 1933 passed a statute with a top levy of only \$50 for the twenty-sixth store and all thereafter.<sup>17</sup> Montana, in its 1935 law went to a

<sup>9</sup> *Ibid.*, 1928, c. 207.

<sup>10</sup> *Laws of Florida*, 1935, c. 16848.

<sup>11</sup> *Laws of California*, 1935, c. 849.

<sup>12</sup> *Session Laws of 1933, Idaho*, c. 113.

<sup>13</sup> *Laws of Pennsylvania*, 1937, Pub. Act 344.

<sup>14</sup> *Laws of Texas*, 1935, c. 400.

<sup>15</sup> *General Laws of Mississippi*, 1936, c. 157.

<sup>16</sup> *Session Laws of 1935, Colorado*, c. 216.

<sup>17</sup> *Laws of Maine*, 1933, c. 260.

maximum of only \$30 for every store in excess of ten.<sup>18</sup> Between these extremes, of course, a great many appear with maximum highs of \$100, \$150, and \$200.<sup>19</sup>

The constitutionality of the various chain-store taxes discussed here will be reserved for treatment in the following chapter. In general, however, it may be said at this point that almost all of the taxes imposed according to the number of stores and graduated on such a basis have been declared constitutional. When the Indiana law was upheld in the case of *Jackson v. Tax Commissioners*, 268 U.S. 527 (1931), the chain stores expressed the opinion that the rather moderate nature of the then existent legislation would not prevail for long. In this they were correctly estimating the future. With official sanction now granted to this method of tax control, state after state proceeded to enact tax measures following roughly the lines established by the Indiana enactment. As time passed the rates were steadily increased, and in 1933 Indiana itself increased the amounts of the tax over the figures set under the original statute.

While the majority of the states continued to follow the Indiana pattern a few were experimenting with other methods of penalizing the chains through taxation.

In 1930 the state of Kentucky passed an act imposing a tax which was graduated as the volume of gross sales at retail increased.<sup>20</sup> Beginning with a tax of one-twentieth of 1 per cent on gross sales of \$400,000 or less the tax was raised to a full 1 per cent on all gross sales in excess of \$1,000,000. The assumption appears to have been that there was some relationship between the volume of such sales and the ability of the stores to pay a higher tax. Undoubtedly there was a remote relationship between the two elements, but the court held that it was too indirect, that the tax was accordingly based upon an arbitrary method of classification, and was for that reason unconstitutional.<sup>21</sup> The tax was not based upon the number of stores in a chain or upon the size of the stores, but purely upon the amount of goods sold,

<sup>18</sup> *Revised Codes of Montana*, 1935, c. 221.

<sup>19</sup> See above, Table 1, p. 9.

<sup>20</sup> *Laws of Kentucky*, 1930, c. 149.

<sup>21</sup> *Stewart Dry Goods Co. v. Lewis*, 294 U.S. 550 (1935).



whether at a loss or profit. While Kentucky was a pioneer in this type of legislation, it was not alone.

Other states began to toy with the idea of combining the two forms of graduated tax against the chains. According to this plan both a tax on the number of stores in the chain and a tax upon the gross sales of the chain were to be imposed.

It was not until 1935 that the Kentucky law was declared unconstitutional, and in the meantime the state of Minnesota, in 1933, enacted one of these combination taxes.<sup>22</sup> Under the Minnesota law a tax of \$5.00 was imposed on all stores in excess of one and under eleven which were owned, managed, or controlled by the same interests. On the eleventh, and all thereafter through the twentieth, a tax of \$15 was levied and graduation took place from that point to a peak of \$155 on the fifty-first store and all over that level. This completed section A of the act. In section B, a tax similar to that imposed in Kentucky was introduced. Rates ran from a low of one-twentieth of 1 per cent on gross sales not over \$100,000 to a high of 1 per cent on all gross sales in excess of \$1,000,000. The act excluded gasoline filling stations, dealers in fuel and lumber and in grain and building material whose sales in the specific items mentioned amounted to not less than 95 per cent of their total sales at retail. The statute also permitted deductions for bad debts in computing the gross sales total for tax purposes. The taxpayer was also permitted to select one of his stores, the sales of which might be excluded from taxation. The purpose of this clause as a legal gesture is evident.

Iowa in 1935 attempted the same program with a range extending from a low of \$5.00 to a high levy of \$155 on the number of stores in the chain and \$1.00 rather than a percentage tax on gross sales under section B of the act.<sup>23</sup> This portion of the statute varied from a low of \$25 on all sales under \$50,000 to a high of \$1,000 on all sales in excess of \$9,000,000. The Iowa law excluded co-operatives, those selling farm products, coal, lumber, ice, grain, feed, building materials, and the sales of liquor stores established and operated by the State Liquor Control Commission, all rooming-houses, and stores located in unincorporated villages where

<sup>22</sup> *Laws of Minnesota, 1933, c. 213.*

<sup>23</sup> *Laws of Iowa, 1935, c. 329.*



no store was more than six miles distant from every other store in the system.

The Iowa law came up for court hearing on November 9, 1936, and the United States Supreme Court declared unconstitutional that portion of the act which imposed the graduated tax on gross sales. The rest of the act was sustained.<sup>24</sup>

Florida in 1935 passed an act similar to the one in Iowa, inasmuch as it taxed both gross sales and the number of stores, but the Florida bill differed from the other combination statutes in the manner in which it taxed gross sales. Here the tax was graduated not in terms of the volume of gross sales but in terms of the number of stores which contributed to the total sales volume. This can be best understood, perhaps, by reference to the following illustration:<sup>25</sup>

| Number of Stores<br>in Chain | Percentage Tax on Gross Receipts<br>from All Sales at Retail |
|------------------------------|--------------------------------------------------------------|
| 1 .....                      | $\frac{1}{2}$ of 1                                           |
| 2-3 .....                    | 1                                                            |
| 4-6 .....                    | 2                                                            |
| 7-10 .....                   | 3                                                            |
| 11-15 .....                  | 4                                                            |
| 16 and over .....            | 5                                                            |

This is section B of the Florida act and is quite apart from section A, which levied a tax the rates of which increased as the number of stores in the chain rose, in line with the Indiana pattern. The Supreme Court of Florida heard the case involving this statute on November 27, 1935, and declared (as the United States Supreme Court was to do one year later in the Iowa case) that the section taxing gross sales at retail was invalid. The remaining sections were considered acceptable.<sup>26</sup>

The Minnesota law, similar to those of Iowa and Florida, had been the first of such measures enacted but the last to appear for court hearing. The explanation for this may lie in the fact that the Minnesota statute was reasonably lenient, at least as com-

<sup>24</sup> *Valentine v. Great Atlantic and Pacific Tea Company*, 57 S.Ct. 56 (1936).

<sup>25</sup> *Laws of Florida*, 1935, c. 16848.

<sup>26</sup> *State ex rel. Adams et al. v. Lee, State Comptroller*, 166 S. 249 (1935).

pared with certain of the measures which the courts had accepted. The chains may have been content to reside under the moderate pressure of a law which they could have defeated, rather than force a court hearing which would have led to its replacement by a judicially acceptable bill which would undoubtedly have been more punitive. At any rate, whatever the reason may have been, the final ruling on the Minnesota statute did not come until December 1, 1937, and the legislature lost no time in introducing another replacing bill of the Indiana type.

It remained for Louisiana to attempt a heavily punitive departure from the accepted pattern, by imposing a tax on all stores under single management located within the state, the tax being computed in terms of the number of stores located within the state or elsewhere. The rates under this act rose from a minimum of \$10 on the first to tenth stores to a maximum of \$550 on all over five hundred. Thus a single store of a large chain having only that one unit in Louisiana would be assessed not \$10, as would be the case in other states, but a much higher figure, perhaps \$550 if there were five hundred or more stores located outside of the state.<sup>27</sup>

This act came up for judicial review on May 17, 1937, and the Supreme Court of the United States indorsed the measure in a four to three decision. While one must hesitate before declaring any event significant, it appears that this Louisiana decision may be every bit as important as was the first favorable ruling of the Supreme Court in *Jackson v. Tax Commissioners*, 283 U.S. 527 (1931). The earlier decision opened the way for the entire wave of anti-chain taxes. This later ruling may pave the way for a new aspect of the anti-chain taxing program.

If the implications of this Louisiana statute are accepted by the other states there appears to be little limit on the amount or extent of the taxes levied against the corporate chains. A slight revision of selected phrases of the existent Indiana-type legislation would extend the taxing base to include all stores in a chain. The computation of store numbers under these measures now includes only those stores in the taxing state. A slight change in the

<sup>27</sup> *Acts of Louisiana*, 1934, No. 51.

wording would extend this to include all stores wherever located, and would increase the tax burden sharply.

The more recent enactments, those of 1937 in particular, have introduced a new aspect to this discriminatory program. The state of Georgia in 1936 passed a bill which levied a graduated tax on mail-order units as well as one on the general group of chains.<sup>28</sup> The mail-order tax was much higher than that on other chains, beginning with a tax of \$2,000 on the first store and moving up to a maximum levy of \$10,000 on the fifth store and all thereafter.

The new Minnesota law, which replaced the one declared unconstitutional in December of 1937, also provided for a levy on mail-order outlets. Here the rates were somewhat lower than those set under the Georgia law, ranging from a low of \$200 on the first unit to a high of \$1,200 on all in excess of ten.<sup>29</sup> In other particulars the statute was similar to the Georgia law.

Montana, in the same year, enacted still another variation of the Indiana-type act. Here a graduated tax was levied on general chains and the same type of tax, at lower rates, was imposed upon filling stations and lumber yards in chain form. Coupled with this was a flat tax of \$37.50 levied against each unit of a wholesaling chain.<sup>30</sup>

The remaining state statutes present several interesting points. The New Mexico law of 1934 in a stern effort to avoid the words "chain store" provided for a tax upon "any person, or persons, firm, association, partnership, stock company, or corporation, having a fixed and established place of business and dealing in merchandise by selling to the ultimate consumer in smaller quantities than that purchased and who sells in small packages, parcels, bales, boxes or other containers." In this fashion the state assembly sought to provide legislation the burden of which would fall most heavily upon the corporate chains but which would eliminate from taxation the independent retailers buying from ordinary wholesalers and dealing through the usual middlemen.<sup>31</sup>

<sup>28</sup> *Laws of Georgia, 1936*, No. 355.

<sup>30</sup> *Laws of Montana, 1937*, c. 199.

<sup>29</sup> *Laws of Minnesota, 1937*, c. 93.

<sup>31</sup> *Laws of New Mexico, 1934*, c. 33.

The majority of the statutes exclude gasoline stations from the provisions of their tax bills, but in some cases this is not true. The West Virginia law specifically applied to filling stations and the courts permitted taxation of such chains, although it was found that they are much more severely penalized by such legislation than the general run of multiple-unit systems.<sup>32</sup>

Co-operative associations are specifically exempted by many of the acts. Other states through the phraseology of their enactments have excluded such groups by implication. The agricultural states tend to omit agencies selling farm produce of their own raising.

Penalties are imposed for failure to pay the license fees and the majority of the laws impose a fine for every day on which a store operates without having paid its required tax. The Colorado law is illustrative of this provision: "For violation of the provisions of this act a penalty of not less than \$200 is levied for each offense and each and every day that such violation continues shall be deemed to be a new offense."<sup>33</sup>

Two of the state acts have been submitted to popular vote. In Colorado, at the general election on November 6, 1934, the popular vote accepted the chain-taxing bill by a count of 197,144 to 155,417. In California chain-store interests succeeded in obtaining a restraining order which prevented the operation of the bill until it could be submitted to a referendum. When the vote was taken in November of 1936 the law was set aside.

Florida in 1931 attempted to impose a tax on chain stores in a bill which drew a distinction between chains operating solely within one county and those operating in more than one county, the latter being taxed at higher rates. This was declared to be an unwarranted type of discrimination and the Supreme Court accordingly ruled the act unconstitutional.

Several of the states, in passing their combination-form taxes covering both sales volume and number of stores, attached a "saving" clause to the effect that court exceptions to any word, phrase, sentence, or section of the given act would invalidate only

<sup>32</sup> *Laws of West Virginia, 1933*, c. 36.

<sup>33</sup> *Session Laws of 1935, Colorado*, c. 216.



the portion to which specific objection was so noted. The remaining portions were to be considered valid.

Some of the states permit the chains to offset other taxes, such as the property tax already paid to the state, against the amount due under the chain-store-tax laws.<sup>34</sup>

The majority of the statutes provide for either semi-annual or annual payments, the latter being more common. One exception might be noted in the case of those earlier bills which computed the tax in terms of the sales volume. These measures required payment twice yearly.

Under the Michigan law of 1935 warehouses or elevators buying, selling, assembling, and shipping farm products were exempted from the provisions of the act.<sup>35</sup>

In the Minnesota law, noted above, provision was made for discounting bad-debt experience in computing the total sales volume. It was necessary, however, that the bad-debts account be kept on an accrual basis. Recoveries obtained were to be added to the gross sales of the next period, the period in which the recovery was made.

Over and above the regular penalties for failure to meet these tax payments certain of the states also provided that unpaid taxes were to bear interest at a given period until settled. The Minnesota act of 1933 set an additional penalty of 1 per cent per month on unpaid portions of the tax bill.

Most of the acts include criminal as well as civil sections. Prison sentences are provided under several of the laws. Mississippi provides for penalties of \$50 to \$100 or thirty days in any county jail or both. In computing the foregoing penalties each and every day upon which such a store remained open was to be deemed a separate offense.<sup>36</sup>

A few of the acts were passed primarily as emergency revenue measures during the depression period and were originally in-

<sup>34</sup> *Public Laws of Vermont, 1933, c. 46, secs. 1123-40.*

<sup>35</sup> *Laws of Michigan, 1935, Part III, c. III, No. 177.*

<sup>36</sup> So far as the writer knows, none of the states have ever enforced the sections providing for criminal punishment.



tended to have only a limited life. The South Dakota law of 1934 was enacted to expire on June 30, 1937. The Wisconsin law of 1933 was to expire on December 31, 1935. The South Dakota law was declared unconstitutional before its expiration date and was replaced with another. The state legislature in Wisconsin, in 1934, enacted another law to take the place of the temporary measure.

Many of the deviations between the acts of the different states can be explained in terms of vested local interests. This is illustrated by the Texas statute of 1935, which excluded oil- and gas-well equipment and supply dealers from the punitive provisions of the act. The Iowa law of 1935 excluded those selling their own farm products. The Mississippi law of 1936 exempted stores or showrooms maintained by utilities for the disposal of gas and electrical appliances.

Since many of the chains have attempted to evade the provisions of these acts by leasing the stores to their managers, some states have sought to cover this contingency. Wisconsin in its 1933 law stated: "Lease and agency and lease and ownership agreements or contracts or operations under a common name shall, unless shown to the contrary, be deemed to constitute operations under the name of the general management, supervision, or ownership."

In the Pennsylvania statute provision is made for approximately the same possibility. Section 6e of the 1937 act holds that two or more stores shall be considered as a chain if any part of the gross revenues or net revenues directly or indirectly inure to the immediate or ultimate benefit of any single person or any group of persons having a common interest therein. This prohibits the chain from leasing the stores to managers—or, apparently, from selling the units to such individuals, then acting as wholesale organizations for such "independent stores."

This completes the discussion of state anti-chain-store tax legislation for the time. There is, however, another aspect of the regulatory program which deserves some attention at this point, the efforts of municipal government to impose chain-store taxes.

## MUNICIPAL CHAIN-STORE TAXATION

City taxation of the chain stores follows closely the pattern set by state legislatures. Scattered attempts had been made during the 1920's to enact such measures, but it was not until 1931 that the first of these ordinances was formally adopted.

The initial measure was passed by Portland, Oregon, in 1931, with taxes ranging from a minimum of \$6.00 per store to a maximum of \$50 on the twentieth unit and all thereafter. Hamtramck, Michigan, levied a tax graduating upward to a high of \$1,000 per store for all over three in a single chain. St. Louis, Missouri, set taxes moving from a low of \$25 on the second store of a chain to a high of \$250 on the twenty-fifth and all beyond that level.

A number of other cities have from time to time passed such measures, although the courts have been inclined to look with some skepticism on such efforts.<sup>37</sup> Among those cities are the following: Red Bank, New Jersey; Durham, North Carolina; Knoxville, Tennessee; Milwaukee, Wisconsin; Youngstown, Cleveland, and Columbus, Ohio; Fredericksburg, Virginia; Atlantic City, New Jersey; Louisville, Kentucky; Huntington, West Virginia; Allentown, Pennsylvania; Georgetown and Columbia, South Carolina; Phoenix, Arizona; and Savannah, Georgia.

Some of the municipalities have passed measures which impose a flat-rate tax of a certain amount per store.<sup>38</sup> The rates are frequently set at different levels for the chains in different fields. The Savannah, Georgia, law of 1935 is illustrative (Savannah Municipal Chain-Store Tax, 1935):

|                                                                    |
|--------------------------------------------------------------------|
| Variety stores, \$500 each, plus \$35 if soda fountain is operated |
| plus 25 if lunches are served                                      |
| plus 25 if flowers, plants, shrubbery are sold                     |
| plus 50 if automobile oil is sold                                  |
| plus 75 if restaurant is operated                                  |
| Total \$710 per store                                              |

Other cities have passed ordinances with a flat tax on gross receipts.<sup>39</sup> Illustrative here is the measure of Huntington, West

<sup>37</sup> *Cincinnati v. Oil Works*, 123 Ohio 448 (1931).

<sup>38</sup> Louisville, Ky., 1933; Savannah, Ga., 1935; Bluefield, W.Va., 1936.

<sup>39</sup> Huntington, W.Va., 1935.

Virginia (upheld by the state Supreme Court in 1936), which imposed a flat tax of one-fourth of 1 per cent of gross receipts.

Allentown, Pennsylvania, in 1933 enacted a modified graduated license tax on the gross sales volume. Rates differed for different types of chains. Merchants paid a tax ranging from \$2.00 on the first \$2,000 of sales to \$100 on sales of \$200,000 and over. Restaurants were covered by a tax ranging from \$5.00 on sales of less than \$2,000 to a maximum of \$25 on sales of \$5,000 and over.<sup>40</sup>

A different tax base was provided by Oakland, California, which imposed a tax of \$6.00 for the first employee on to \$1.00 for each between 11 and 310 and 50 cents for all beyond that level.<sup>41</sup>

A flat-rate license tax was coupled with one having graduated rates in Atlantic City, New Jersey. Chain variety stores paid a flat \$150 per unit, department store units were assessed \$200 a year, and restaurant chains paid a graduated tax ranging from a low of \$15 to a high of \$120 a year. Here the graduation was computed in terms of the number of tables.<sup>42</sup>

The Durham, North Carolina, law is interesting, inasmuch as it appears to have been inspired by a section of the state anti-chain bill (*Laws of North Carolina, 1935, No. 30*). The state taxing bill says: "Counties shall not levy a license tax on the business taxed under this section but cities and towns may levy a license tax not in excess of \$50 for each store in a chain located in such city or town." The Durham ordinance imposed a flat tax of \$50 on each store in excess of one and coupled this exaction with a graduated gross-sales tax on merchants not subject to the state chain-store tax.<sup>43</sup>

Fredericksburg, Virginia, passed a chain-store-tax bill setting flat rates of \$250 for each store over one.<sup>44</sup> This bill was held invalid by a lower court in Virginia in 1935, but on appeal was upheld by the state Supreme Court in March of 1937.

<sup>40</sup> Allentown, Pa., 1933. Others enacting generally similar ordinances were: Columbia, S.C., 1935; Georgetown, S.C., 1935; Phoenix, Ariz., 1935.

<sup>41</sup> Oakland, Calif., 1933.

<sup>42</sup> Atlantic City, N.J., 1935. A similar bill may also be found in Kansas City, Mo., 1935.

<sup>43</sup> Durham, N.C., 1934-35.

<sup>44</sup> Fredericksburg, Va., 1933.

A new type of municipal ordinance was introduced by Augusta, Georgia, in December, 1938. It was built along the lines established by the chain tax of the state of Louisiana. The rates were to graduate with an increase in the number of stores wherever located. Rates rose to a maximum of \$100 for each store in Augusta belonging to a chain having 150 or more stores in that city or elsewhere.<sup>45</sup>

What the future holds for municipal tax measures is debatable. The courts have accepted some and rejected others, but no clear-cut pattern appears to have been established. If the courts do adopt a favorable attitude the future of the chain stores will become even less enticing than it now appears under state legislation.

#### FEDERAL ANTI-CHAIN-TAX PROPOSALS

It is significant to note that the federal government has had under consideration two specific bills patterned somewhat upon the lines of the state taxing statutes. The federal House of Representatives on June 8, 1937, accepted by an overwhelming vote (155 to 43) an amendment to the District of Columbia appropriation bill, a chain-store-taxing provision which would have established a graduated tax along the lines of the Louisiana statute, attaining a high of \$550 for all chains of more than 100 units. The tax would have been imposed on each store of such a chain located in the District of Columbia. The proposal was defeated in the Senate, but is significant in that it denotes a strong anti-chain sentiment in the lower house.

On February 14, 1938, Representative Patman, co-author of the Robinson-Patman bill, introduced in the House a bill which would impose a graduated tax on chain stores throughout the nation. Seventy-five other representatives appeared as co-sponsors.

The proposed statute provided for a tax of \$50 per store on chains having 9 to 15 units; a tax of \$100 per store on chains having 16 to 25 units; \$200 per store on 26 to 50 unit chains, and so

<sup>45</sup> Augusta, Ga., 1938.



on up to a maximum levy of \$1,000 on each store of a chain having more than 500 units. In addition to the foregoing, the bill provided for the complete extermination of all large chains of national scope by an additional section which requires a chain operating in more than one state to multiply the applicable tax by the number of states in which the chain operates.

Chains whose gross annual sales amounted to less than \$250,000 were to be exempt, as were those having fewer than nine stores. During the first year of its operation the proposed bill would levy these taxes at rates amounting to 50 per cent of the full stated rates provided. In the second year the figure would move up to 75 per cent, and the full levy would be achieved in the third year after enactment. This was presumably introduced in order to give the chains time in which to wind up their affairs short of complete disintegration. Mr. Patman has frankly stated that the intention of his proposal is to drive the large chains out of existence.<sup>46</sup>

#### SUMMARY

It has been eleven years since the first of these enactments was passed, and in the course of that time the movement has grown until, at the present time, there are discriminatory tax measures in exactly one-half of the states. The high point of the movement was apparently reached in 1933, when thirteen states enacted taxing bills. No statutes were passed in 1938, the first blank year since the inception of the program in 1927. This last year was, however, an off-legislative one and 1937, when a majority of the state assemblies were in session, witnessed the passage of eight such statutes and saw the movement taking shape in the highly industrialized states for the first time. Table 3 indicates the growth of these taxes year by year.

The movement has spread from the states to the municipalities,

<sup>46</sup> "A. & P. Fights Patman," *Chain Store Review: Groceries*, November, 1938, pp. 23-26, and in particular p. 24, where the following appears: "The Honorable Wright Patman, representative in Congress of the first district of Texas, has announced that he will introduce in the next Congress a punitive and discriminatory tax bill frankly designed to put chain stores out of business."



where extremely punitive measures have been the rule. Court relief may come to the aid of the chains in the case of these city ordinances, although the position is by no means settled at the present time.

TABLE 3\*  
NUMBER OF DISCRIMINATORY CHAIN-STORE-TAXING  
BILLS BY YEAR OF ENACTMENT, 1937-38

| Year      | Number<br>Passed | Year      | Number<br>Passed |
|-----------|------------------|-----------|------------------|
| 1927..... | 3                | 1933..... | 13               |
| 1928..... | 2                | 1934..... | 4                |
| 1929..... | 4                | 1935..... | 7                |
| 1930..... | 3                | 1936..... | 1                |
| 1931..... | 5                | 1937..... | 8                |
| 1932..... | 3                | 1938..... | 0                |

\* Sources: statutes and code books of the various states.

While the federal government has not yet enacted such a bill, two chain-taxing measures have been before Congress, one for the District of Columbia, the other a proposal to tax chains on a nation-wide front.

### CHAPTER III

#### COURTS AND CHAIN-STORE TAXES

THE period prior to 1929 may be considered as the experimental stage of the chain-store-tax movement, as a period in which preliminary attempts were made to chart a course through hitherto untraveled waters. Today, while there are still a number of unsettled questions concerning these chain-store taxes, a general pattern seems to have been outlined by the numerous court decisions of the past decade. A body of positive and negative rulings has been established sufficient to effect some crystallization of the mold.

#### EARLY CASES

The most important of the early cases involving chain-store taxation was that which arose in connection with the first Indiana bill (*Public Laws of Indiana, 1928, c. 207*). This act imposed a tax which increased progressively as the number of stores in the chain increased, until a maximum rate was reached at the level of the twenty-first store. This top levy was \$25.

The chain-store interests of the state, as represented by the owner of the Standard Grocery Company of Indianapolis, L. A. Jackson, instituted proceedings in the three-judge Statutory Court of the Southern District of Indiana to enjoin enforcement of the act. This court, after hearing evidence on the case, decided that the statute constituted a violation of the equal-protection clauses provided by state and federal constitutions. The act was accordingly declared unconstitutional.

At this point the proponents of the bill appealed to the United States Supreme Court, where the measure was argued on March 5, 1931, and a decision rendered two months later on May 18.<sup>1</sup> The appellee, the tax commission, pleaded violations of the federal and state constitutions had not occurred and argued that the

<sup>1</sup> *State Board of Tax Commissioners of Indiana v. Jackson*, 283 U.S. 527 (1931).

statute was an ordinary revenue bill; that it had been imposed under the provisions of the Constitution which permitted the state to enact legislation for the purpose of raising revenue; that the tax was nothing more than an occupational levy, an assessment which the state was allowed to make.

The appellant, Jackson, contended that the act was a violation of federal and state constitutional requirements and argued that the act was based on the following instances of arbitrary discrimination:

1. That the graduation of the rate of tax as the number of stores under single management and ownership increased was based on no real differences between store and store, where one is part of a group and one is individually owned and operated. Nor was it based upon any real differences in the nature of the business transacted within such stores.

2. That the number of stores bears no relation to the public health, welfare, or safety, hence such a tax cannot be supported on the belief that it is enacted under the police power of the state.

Both parties to the case introduced factual evidence to support their conflicting contentions concerning the existence of real differences between stores operated as part of a chain system and stores independently owned and operated.

The court by a five to four decision overruled the injunction of the lower court, holding the act to be well within the powers of the state, and said:

The power of taxation is fundamental to the very existence of government of the states. The fact that a statute discriminated in favor of a certain class does not make it arbitrary, if the classification is founded upon a reasonable basis or if any state of facts can reasonably be conceived to sustain it.

If the selection or classification is neither capricious nor arbitrary and rests upon some reasonable consideration or difference or policy there is no denial of equal protection of the law.

This statute treats upon a similar basis all owners of chain stores similarly situated.

The judgment of the District Court must be reversed and remanded with instructions to dismiss the bill. There is a real difference between a system of stores under one management or supervision and a store singly owned and operated.

The concluding sentence of this portion of the decision is important. Upon the phrasing of that passage rests nearly all of the permitted forms of chain-tax legislation. By holding that there are real differences between chain and independent stores the Supreme Court made possible the use of discriminatory tax legislation. With this decision as a precedent state courts were forbidden to find such legislation per se arbitrarily discriminatory.

The decision presented another of the famous five to four divisions of the Supreme Court. Justices Van Devanter, McReynolds, Butler, and Sutherland dissented, and Mr. Justice Sutherland wrote the dissenting opinion, which bears quoting in part:

It may be that here the minimum tax of \$25 for each store, while relatively high, is not if considered by itself, excessive; but to sustain it will open the door of opportunity to the state to increase the amount to an oppressive extent. This court has frequently said—and it cannot be too often repeated in cases of this character—that the power to tax is the power to destroy; and this constitutes a reason why that power, however moderately exercised in given instances, should be jealously confined to the limits set by the Constitution.

In the face of this decision and others which might have been cited there does not seem to be any sure comfort in the suggestion sometimes made that this court may be expected to intervene whenever the tax reaches the point of destruction. For the foregoing reasons the judgment of the three judge Federal Court of Indiana declaring this tax unconstitutional should be affirmed.

Without entering into a discussion of the legal value of Mr. Justice Sutherland's opinion one or two suggestive points may be noted. "The power to tax is the power to destroy," while not a new legal doctrine in constitutional law, is one of the major aspects of the constitutional analysis of chain-taxing legislation. By declaring that a given method of imposing levies upon such groups is constitutional the way is opened for increased exactions under the same pattern. Whether the court will intervene if the rate of such taxes becomes excessive is a point upon which the dissenting opinion expressed uncertainty. Just where the limitation begins is, of course, a matter to be decided for each case as it arises and no generalization can be permitted. Some possible help may be found in the action taken by the same United States Supreme Court



in the California Caravan Case (May 3, 1937), where certain definite limitations were placed upon the rates of taxation to be applied. This case, testing the right of the state of California to impose a tax of \$15 on all automobiles coming into the state, caravan fashion, caused the court to agree that while a state had the right to regulate the use made of its highways, and might choose to do this through exercise of its taxing power, it could tax only to that level which would be sufficient to regulate. Beyond that point it could not go. It might force the group regulated to pay a duty sufficient to cover all costs of regulation, but not more than sufficient to effect the necessary degree of control.

Be that as it may, time has proved Mr. Justice Sutherland correct in his predictions. Year by year the rates have been increasing, and Indiana itself, two years after the date of this decision, increased its rate sixfold, from \$25 to \$150.

If one were asked to pick the case among all of the many involving the power of the states to tax discriminately the operation of chain stores the task might be somewhat difficult. If, however, one were required to select the two essential cases this one from Indiana would demand consideration. In the Jackson case the official approval of the United States Supreme Court was given to such statutes. From the time of this decision and on down to the present the chains have met with little success in their attempts to overthrow discriminatory state taxes. This held true without exception for every state act passed in conformance with the pattern set in Indiana.

#### COURTS AND THE INDIANA-TYPE LEGISLATION

Another case, concerning a law modeled roughly along the lines of the Indiana statute, but modified in one major respect, came up from the state of Florida on appeal from the Supreme Court of that state.

Florida in 1931 passed an act (*Public Laws of Florida, 1931, c. 15*) which imposed a graduated tax on the chain stores, increasing the tax-rates as the number of stores increased. Up to this point it was a direct copy of the Indiana law, but an important distinguishing feature was added. If all of the stores of a

given chain were located in one county of the state, that chain was to pay a lower tax than another of the same size whose stores were located in more than one county.

The statute was immediately carried into the Florida courts by the Liggett Drug Store Company, which charged that the imposition of higher taxes upon chains operating in more than one county was so arbitrary as clearly to violate the uniformity and equal-protection clauses of both federal and state constitutions. The Florida court ruled in favor of the state and the drug chain immediately appealed to the Federal Supreme Court for relief.<sup>2</sup>

The court examined the statute, took cognizance of the pleas of the state that the legislature had passed the bill under its revenue powers, noted also that the act might be a potential provider of revenue, then stated that the raising of revenue was not the primary purpose of the bill regardless of what the legislature might have declared, but was only a guise through which something more than that was being attempted. The question then arose as to whether this case should be decided under the same ruling which guided the court in the Indiana case. The majority of the court held that it could not. Admitting the right of a state to classify groups for taxing purposes, the court stated that the classification must be reasonable and just and must not treat two groups in different fashion when primarily they were the same.

Following this line of thought no other decision was possible in the minds of the majority than a ruling favorable to the chain stores. The act was declared invalid, principally because of that section which imposed "heavier license taxes where multiple stores of a single owner are located in more than one county." This was deemed no reasonable basis for classification.

The case made no great law, merely indicating the refusal of the court to accept every type of classification which might be made by the legislators in their drive to penalize the chains. It is, however, one of the significant cases in the panel of chain-tax hear-

<sup>2</sup> *Liggett v. Lee*, 288 U.S. 517, 586 (1932), in which much of Mr. Justice Brandeis' philosophy in the Quaker City Cab Co. case was carried over by him into the extended analysis of corporate forms, bigness in industry, and the social nature of the chain stores.

ings, simply because in this case Mr. Justice Brandeis went to some length in his minority opinion to present what he considered to be the justification for the chain-store taxes in general.

The dissenting opinion was three times as long (forty pages) as the majority opinion. Furthermore, Mr. Justice Stone and Mr. Justice Cardozo, who also dissented, collaborated in another dissenting opinion of six pages. While no detailed quotations from either of these belong here, a few paragraphs are in order at this time. Mr. Justice Brandeis said:

"No one has proven that this is not a reasonable classification under conditions prevailing in Florida. The presumption of constitutionality must prevail in the absence of some factual foundations of record for overthrowing the statute."

Here was expressed a position taken constantly by Mr. Justice Brandeis. A law must be proved unconstitutional, not constitutional. In other words, the burden of proof must always rest upon those who would overthrow, rather than those who would sustain, a given statute.

The state's power to apply discriminatory taxation as a means of preventing domination flows from the broader rights of Americans to preserve and to establish from time to time such institutions, social and economic, as seem to them desirable; and likewise to end those which they deem undesirable.

The citizens of the State, considering themselves vitally interested in this seemingly unequal struggle have undertaken to aid the individual retailers by subjecting the owners of multiple stores to the handicap of higher license fees. They may have done so merely to preserve competition. But their purpose may have been a broader and deeper one. They may have believed that the chain store, by furthering the concentration of wealth and power, and by promoting absentee ownership of wealth is thwarting the American ideals; that it is making impossible equality of opportunity.

This, then, is Justice Brandeis' justification for the chain-store-tax legislation. An interpretation such as the above would seem, if carried to its logical conclusion, to bring these taxes within the police power of the several states, rather than confining such enactments to the exercise of the revenue power alone. This would, of course, broaden considerably the control which the states would be able to exert over not only the chain stores but

also over big business in general. While this was not the opinion of the court it should be noted that Mr. Justice Brandeis' minority opinions have the embarrassing capacity of being remarkably prophetic of the majority opinions at a later date.

#### CASES INVOLVING A GRADUATED TAX ON GROSS SALES

Another class of cases began to appear at about the time the law had become settled with regard to this first group. These involved the acceptability of chain-store taxes which set rates graduated as the volume of gross sales of the chain increased. The first, and foremost, of these cases was that introduced to decide the constitutional position of the Kentucky chain-store tax (*Laws of Kentucky, 1930, c. 149*).

This statute imposed a tax beginning with a rate of one-twentieth of 1 per cent on gross sales of less than \$400,000 and rose to a maximum of a full 1 per cent on gross sales in excess of \$1,000,000. Sales of the entire organization were to be considered and not those of each store individually. State jurisdiction extended, of course, only to those stores of a chain which were within the state.

Suit was brought by the Stewart Dry Goods Company, with the Levy Stores, J. C. Penney Company, and the Kroger Grocery and Baking Company as coplaintiffs. It was charged that the act was unconstitutional, that it was arbitrarily discriminatory, that there was no reasonable relationship between a large volume of gross sales and ability to pay a large tax. The chains argued that it was false to assume that a small volume of gross sales meant of necessity little ability to pay taxes. The state countered this point with a flat denial of the pleas of the chains, arguing in rebuttal that there was a definite relationship between a large volume of gross sales and the net profit thereon, that a larger volume gave a greater proportional net profit than did a small volume, hence a greater ability to pay, and that this was sufficient justification for discrimination in rates as between those with a small and those with a large volume of gross sales.

The court examined the contentions of the parties, and after



weighing the evidence gave a decision which favored the chains. Quoting from the opinion:<sup>3</sup>

It is not the concern of the court to study the name or words of an act, but to ascertain the nature and effects thereof.

This was given in answer to the claim made by the state that the act was merely a sales-tax statute, and as such clearly within the powers of the state.

This statute is a tax on the sale of an article and such a tax constitutes a tax on the article itself.

The evidence is not sufficient to support the contention that the tax was adjusted with reasonable approximation to the net earnings of the taxpayer.

The allegation that a graduated gross sales tax is less complicated and easier of administration than a tax on income is no justification therefore.

The court was divided on this opinion and a dissenting expression was written by Mr. Justice Cardozo, concurred in by Mr. Justice Stone and Mr. Justice Brandeis. A quotation from that opinion follows, indicating the sentiment of that section of the court which had been the consistent supporter of the anti-chain movement.

Even a small difference in the method of conducting business may be availed of by the government in imposing different taxes.

The definiteness with which the court expressed its condemnation of this statute forestalled all later attempts to place such measures on the statute books. Some of the states, however, sought to raise this form to a constitutional position by combining it with the Indiana-type statute. Under such acts levies were imposed at graduated rates on both the number of stores and the volume of gross sales.

Such an act was passed in Wisconsin in 1933 (*Laws of Wisconsin, 1933*, c. 469). A tax of \$10 was levied on the second to fifth stores of a chain and a maximum tax of \$100 was established for all stores over twenty. Combined with this was a tax on gross sales ranging from a low of six-twentieths of 1 per cent to a high of thirteen-twentieths of 1 per cent on gross sales of \$5,000,000 or over.

Protest was immediately filed and the case was carried to the

<sup>3</sup> *Stewart Dry Goods Co. v. Lewis*, 55 S.Ct. 525 (1935).



state Supreme Court on appeal from a decision of the trial court where the act had been upheld. The Supreme Court gave its decision on June 4, 1935. Plaintiff contended that the act was a violation of Section I of Article VIII of the state constitution and of the Fourteenth Amendment to the federal Constitution—in short, a violation of uniformity and equal-protection clauses.

The court said, in ruling the act unconstitutional, that it . . . creates a so called "occupational tax on chain stores" which requires the operators of two or more stores or mercantile establishments, or places where goods, wares or merchandise are sold or offered for sale at retail to pay an annual tax on the gross income derived by such operators from their retail operations in Wisconsin.

[The act] in imposing a graduated tax on gross income is so arbitrary, so unreasonable and discriminatory that it denies to plaintiffs the equal protection of the laws guaranteed by the Fourteenth Amendment.

There is no constant or reasonable relation between gross income and net income, or between gross income and the size in so far as the number of stores is concerned, of an integrated chain or between its gross income and its ability to pay a tax imposed at rates increased progressively for the higher brackets of income; and there is no reasonable relation between such graduations in the rate of taxation and the actual relative value to the parties taxed of the privilege which is enjoyed by each of them as an operator of a chain store and which constitutes the subject taxed.

The decision, given in favor of the appellee, invalidated the entire act because of the discriminatory features of one portion, that which taxed the volume of gross sales. The court indicated that there was no question of separability as between the parts of the act which might have been constitutional and those which were not. With the two inseparable, the tax on the number of stores must fall with the failure of the other section.<sup>4</sup>

#### RECENT ANTI-CHAIN-TAXING CASES

The next case involves questions of constitutionality with regard to a unique measure, the Louisiana statute of 1934 (*Public Laws of Louisiana, 1934*, No. 51). Under this bill a tax similar to that imposed in Indiana was levied against the chain stores of the state. It ranged from a low of \$10 on stores of a chain of ten or less outlets to a high of \$550 for units of a chain having more than

<sup>4</sup> *Wadhams Oil Co. v. Henry*, 218 Wis. 506 (1935).

five hundred stores under single management. This tax differed from the others, however, in that it collected the tax from all stores within the state, but based the computation of the tax on the total number of units in the chain, wherever located. In the other acts the tax had been computed in terms of the number of stores of a chain located within the taxing state. For purposes of calculating the tax in Louisiana, the total number of stores in a chain is used and that rate, applicable to the total number, is then levied against each unit of the chain which is located in Louisiana. If a given chain had one store in Louisiana and five hundred elsewhere, the tax on the single Louisiana store would be \$550.

This case involved a new issue, the right of a state to impose a tax upon a store or group of stores operating within the state, the tax being based upon the number of stores with which there was any affiliation whether within or outside the taxing state.

The measure was contested by the Great Atlantic and Pacific Tea Company and eventually came before the Supreme Court of the United States in the spring of 1937, at which time a decision was given upholding the constitutionality of the act.<sup>5</sup> The case originally arose in the District Court for the Eastern District of Louisiana, where the act had been upheld as constitutional (16 Fed. Supp. 499), and was being appealed by the Great Atlantic and Pacific Tea Company to the highest federal court. Plaintiff contended that the act violated both federal and state constitutions as to uniformity, due process, and equal protection of the laws, and was quite definitely a case in which the state had exceeded its powers. The particular instance of discrimination protested was "an arbitrary discrimination in favor of local as against national chains."

The issue is well outlined in the following quotations from the opinion of the majority of the court:

The Great Atlantic and Pacific Tea Company . . . owning, operating, or controlling 15,082 stores in the United States, Canada and elsewhere, 106 of which are in Louisiana, filed its bill in the District Court to restrain the appellee from enforcing the statute . . . case was heard upon pleadings and

<sup>5</sup> *Great Atlantic and Pacific Tea Company et al. v. Alice Lee Grosjean, Supervisor of Public Accounts*, 57 S.Ct. 722 (1937).

proofs by a specially constituted court of three judges, which upheld the statute and dismissed the bill.

The constitutional infirmity of the act is said to consist in arbitrary discrimination in favor of local as against national chains, in the attempts to tax property and activities which are beyond the state's jurisdiction, and in burdening interstate commerce. We hold the legislation impregnable on these grounds.

The basic points upon which the appellant contested the act are suitably indicated in these passages. In addition to such grounds as were noted the chain store attempted to produce evidence showing the manner in which the act interfered with interstate commerce. The Supreme Court could see no basis for upholding such contentions and said:

First, the exaction is an occupation or license tax. The subject is the conduct of a business within Louisiana. Without contravening the equal protection clause of the Fourteenth Amendment a state may separately classify for taxation the conduct of a chain store and may increase the rate in proportion to the increase in the number of stores<sup>6</sup> within the state, since the opportunities and powers of a chain store operator become greater with the growth of the number of units maintained.

In addition . . . all of the stores of a retail chain contribute to the central purchasing power of the chain, irrespective of state lines, and location of stores and increase the per cent multiple advantage enjoyed by the operator of the system.

If the competitive advantages of a chain increase with the number of its component links, it is hard to see how these advantages cease at the state boundary.

The court's findings are supported by evidence bearing upon a variety of advantages enjoyed by large chains which are unavailable to smaller chains.

The record discloses what would be plain enough without evidence, that generally volume of purchasing spells lower prices, special terms, and other advantages.

It is enough that the classification has reasonable relations to the differences in the practices of small and large chains. The statute bears equally on all who fall into the same class, and this satisfies the guaranty of equal protection.

Second, the appellants contend that the act deprives them of property without due process of the law, because the tax is imposed at least in part upon things which are beyond the jurisdiction of Louisiana.

The tax is laid solely upon intrastate commerce. In the exercise of police

<sup>6</sup> This, of course, is the point already well settled by a number of cases, among which the Indiana decision stands forth (*Tax Commissioners v. Jackson, op. cit.*).

power the state may forbid as inimical to the public welfare the prosecution of a particular business or regulate the business in such manner as to abate evils deemed to arise from its pursuit. Whatever a state may forbid or regulate it may permit upon condition that a fee be paid in return for the privilege, and such a fee may be exacted to discourage the prosecution of a business or to adjust the competitive or economic inequalities.

The judgment of the District Court is affirmed.

This was another of the closely divided decisions which have prevailed in these chain-store-tax cases. Justices Van Devanter and Stone did not sit on the case, and of the remaining seven justices, three dissented from the majority opinion—Sutherland, McReynolds, and Butler. They collaborated in one dissenting opinion, concerned chiefly with the channels which the majority decision opened for future taxation of the chains.

Perhaps one of the most important passages in the majority opinion is that beginning "In the exercise of the police power. . . ." This, while not a particularly new interpretation of the police power of a state, is important as applied to the chain-store-tax legislation, for it immeasurably widens the scope of state control over the chains. Prior to this decision the chain-store-taxing bills had been enacted under the revenue powers of the states.

In certain of the earlier cases it will be remembered that the courts went into considerable detail in stating that there was no question of public health, welfare, or safety. It had, consequently, been impossible to justify these measures in terms of the police power. Acceptability, if realized, had to come under the revenue power. A Supreme Court precedent appears to have been established by this Louisiana ruling whereby legal justification of such acts will follow under the police power. It is impossible to indicate at this point the full magnitude of the decision, but that it does greatly amplify the degree of state regulatory control is certain.

Nor will it be amiss at this time to refer to the position taken by Mr. Justice Brandeis in the first Florida case (*Liggett v. Lee*, cited above) in 1932. Consistent with past experience, a Brandeis minority opinion has again become the opinion of the majority—this time after the passing of only five years.

While the states have not as yet begun to adopt this extremely



punitive Louisiana-type statute, the situation, in so far as the larger corporate chains is concerned, is anything but wholesome. If, as the court said, "it is hard to see how these advantages cease at the state boundary," then there is no restriction upon the rights of the state governments to drive all save the smaller local or sectional chains from the scene.

What conclusions are warranted concerning the significance of this decision? By broadening the police power of the states to include such legislation it has certainly made possible a much more intensive type of control than was possible prior to this decision. Second, by specifically permitting the type of statute enacted in Louisiana, it leaves the future of the chain store quite completely within the hands of the state legislators.<sup>7</sup> Finally, and perhaps most important of all, are the implications found in this decision pointing to a much more hostile attitude on the part of the Supreme Court. Mr. Justice Brandeis, formerly in the minority on many of the earlier cases, began to find himself on the side of the majority, and the change occurred not in the position of Mr. Justice Brandeis, but in that taken by the other members of the court.<sup>8</sup>

<sup>7</sup> While this may appear to be a somewhat debatable point, it should be remembered that there is always the possibility that another Supreme Court, at a later date, may invalidate the present decision in much the same manner that the Supreme Court of 1920 overruled the decisions of the earlier courts in matters of anti-trust regulation and prosecution.

<sup>8</sup> As this material went to press it was announced that the Pennsylvania Supreme Court had, on June 19, outlawed the chain tax in that state. Three months earlier the Kentucky levy was voided by the Court of Appeals of that state (March 21, 1939). The Minnesota law of 1933 finally reached the state Supreme Court (although officially repealed by the chain store tax of 1937) and was declared unconstitutional in June of 1939. Thus all of the cases heard in the first half of 1939 presented verdicts favorable to the chains.

## CHAPTER IV

### REGULATORY EFFECT OF CHAIN-STORE TAXES

THE criteria by which these chain-store-taxing statutes are to be evaluated must, of necessity, be somewhat complex. In a sense they present standards which are irreconcilable. There are many conflicting interests at stake. If the taxes fully satisfy certain of the requirements they will partially fail to come up to the standards set by others. Inasmuch as one of the principle motives for the enactment of these taxing bills appears to be the desire to penalize corporate chain existence, it is from this point of view that the present chapter is written.

#### CASE I

The Indiana bill, which is quite typical of the group it represents, will now be taken and its application to one chain, the F. W. Woolworth organization, will be considered.

The provisions of the Indiana statute of 1933 establish the tax levies shown in the accompanying table.

| Number of Stores | Tax  |
|------------------|------|
| 1.....           | \$ 3 |
| 2-5.....         | 10   |
| 6-10.....        | 20   |
| 11-20.....       | 30   |
| 21 and over..... | 150  |

This is the tax which is to be imposed, in Case I, by all of the states. The F. W. Woolworth chain, a large national organization, is to be subjected to this tax burden. In order to analyze the impact of this measure the situation will have to be considered state by state, since the Indiana law, for purposes of tax computation, counts only the stores in the taxing state. It will, therefore, be necessary to obtain data on the number of stores operated by the Woolworth Company in each state. This is presented in Table 4.

Here in Case I an attempt is being made to portray the effects

of the Indiana chain-store tax upon national, as over against local and sectional, chains. For purposes of this case it is apparent that the F. W. Woolworth Company is an ideal subject, with stores located in each of the forty-eight states.

One or two words of explanation may be in order at this time as to the method of handling the data. It would not be correct when

TABLE 4  
DISTRIBUTION OF WOOLWORTH COMPANY STORES

| State                   | Number<br>of Stores | State                    | Number<br>of Stores |
|-------------------------|---------------------|--------------------------|---------------------|
| Alabama . . . . .       | 17                  | Nebraska . . . . .       | 18                  |
| Arizona . . . . .       | 8                   | Nevada . . . . .         | 1                   |
| Arkansas . . . . .      | 9                   | New Hampshire . . . . .  | 12                  |
| California . . . . .    | 117                 | New Jersey . . . . .     | 69                  |
| Colorado . . . . .      | 20                  | New Mexico . . . . .     | 4                   |
| Connecticut . . . . .   | 25                  | New York . . . . .       | 225                 |
| Delaware . . . . .      | 2                   | North Carolina . . . . . | 24                  |
| Florida . . . . .       | 15                  | North Dakota . . . . .   | 8                   |
| Georgia . . . . .       | 16                  | Ohio . . . . .           | 109                 |
| Idaho . . . . .         | 9                   | Oklahoma . . . . .       | 19                  |
| Illinois . . . . .      | 182                 | Oregon . . . . .         | 14                  |
| Indiana . . . . .       | 40                  | Pennsylvania . . . . .   | 151                 |
| Iowa . . . . .          | 41                  | Rhode Island . . . . .   | 10                  |
| Kansas . . . . .        | 26                  | South Carolina . . . . . | 8                   |
| Kentucky . . . . .      | 19                  | South Dakota . . . . .   | 8                   |
| Louisiana . . . . .     | 14                  | Tennessee . . . . .      | 20                  |
| Maine . . . . .         | 21                  | Texas . . . . .          | 56                  |
| Maryland . . . . .      | 18                  | Utah . . . . .           | 4                   |
| Massachusetts . . . . . | 116                 | Vermont . . . . .        | 9                   |
| Michigan . . . . .      | 75                  | Virginia . . . . .       | 26                  |
| Minnesota . . . . .     | 46                  | Washington . . . . .     | 22                  |
| Mississippi . . . . .   | 16                  | West Virginia . . . . .  | 18                  |
| Missouri . . . . .      | 63                  | Wisconsin . . . . .      | 56                  |
| Montana . . . . .       | 13                  | Wyoming . . . . .        | 5                   |

computing the tax burden in any given state to take the total number of stores, then multiply that number by the tax-rate applicable at such a level. The tax is not established in that fashion. It is a cumulative affair; as the number of stores in a state increases the rate on each added store becomes higher than that on earlier units. Thus the tax-rate on each store in, for example, Utah would be much lower than the rate per store in New York. Furthermore, it would be incorrect to take the seventeen stores in Alabama, check them with the statute, discover that the taxing

provisions impose a levy of \$30 on all stores between eleven and twenty, then multiply the number of stores, 17, by the \$30 figure. Such a result would be erroneous. The tax correctly computed for Alabama would be as shown in Table 5.

For all stores over twenty the tax is a flat \$150 per store under the Indiana law. To facilitate computation a table is presented in the footnote below<sup>1</sup> giving the total tax bill at all levels up to the twentieth store. The application of the proper rates, as indicated

TABLE 5  
COMPUTATION OF THE TOTAL TAX PAID  
BY WOOLWORTH IN ALABAMA

| Number of Stores    | Tax Rate (Each) | Cumulative Tax |
|---------------------|-----------------|----------------|
| 1.....              | \$ 3            | \$ 3           |
| 2-5.....            | 10              | 40             |
| 6-10.....           | 20              | 100            |
| 11-17.....          | 30              | 210            |
| Total tax bill..... |                 | \$353          |

in the footnote will establish the following tax levies for the F. W. Woolworth Company, state by state.

These are the figures for the Woolworth chain in each state. They range from a low average of \$3.00 for the one store operated in Nevada to a high figure of average per-store tax of slightly more than \$139 in the state of New York. The total amount to be paid by the chain under this statute, if effective in all states, would be

<sup>1</sup> The following table may be used to facilitate the calculation of tax levies.

INDIANA TAX RATE COMPUTED CUMULATIVELY FOR  
ANY NUMBER OF STORES TO TWENTY

| Store Number | Tax-Rate | Total Tax | Store Number | Tax-Rate | Total Tax |
|--------------|----------|-----------|--------------|----------|-----------|
| 1.....       | \$ 3     | \$ 3      | 11.....      | \$30     | \$173     |
| 2.....       | 10       | 13        | 12.....      | 30       | 203       |
| 3.....       | 10       | 23        | 13.....      | 30       | 233       |
| 4.....       | 10       | 33        | 14.....      | 30       | 263       |
| 5.....       | 10       | 43        | 15.....      | 30       | 293       |
| 6.....       | 20       | 63        | 16.....      | 30       | 323       |
| 7.....       | 20       | 83        | 17.....      | 30       | 353       |
| 8.....       | 20       | 103       | 18.....      | 30       | 383       |
| 9.....       | 20       | 123       | 19.....      | 30       | 413       |
| 10.....      | 20       | 143       | 20.....      | 30       | 443       |



\$178,674, an item which would have to be added to the fixed costs of the chain so long as it continued to do business in its existent form. With a total of 1,824 stores in the forty-eight states, the average amount paid per store is \$97.96. This means, everything else being the same, that an average store would sacrifice approxi-

TABLE 6  
F. W. WOOLWORTH CHAIN-TAX BILL UNDER A NATION-  
WIDE INDIANA CHAIN TAX

| State                   | Amount<br>of Tax | State                    | Amount<br>of Tax |
|-------------------------|------------------|--------------------------|------------------|
| Alabama . . . . .       | \$ 353           | Nebraska . . . . .       | \$ 383           |
| Arizona . . . . .       | 103              | Nevada . . . . .         | 3                |
| Arkansas . . . . .      | 123              | New Hampshire . . . . .  | 263              |
| California . . . . .    | 14,993           | New Jersey . . . . .     | 7,793            |
| Colorado . . . . .      | 443              | New Mexico . . . . .     | 33               |
| Connecticut . . . . .   | 1,193            | New York . . . . .       | 31,193           |
| Delaware . . . . .      | 13               | North Carolina . . . . . | 1,043            |
| Florida . . . . .       | 293              | North Dakota . . . . .   | 103              |
| Georgia . . . . .       | 323              | Ohio . . . . .           | 13,793           |
| Idaho . . . . .         | 123              | Oklahoma . . . . .       | 413              |
| Illinois . . . . .      | 24,743           | Oregon . . . . .         | 263              |
| Indiana . . . . .       | 3,443            | Pennsylvania . . . . .   | 20,093           |
| Iowa . . . . .          | 3,593            | Rhode Island . . . . .   | 143              |
| Kansas . . . . .        | 1,345            | South Carolina . . . . . | 103              |
| Kentucky . . . . .      | 413              | South Dakota . . . . .   | 103              |
| Louisiana . . . . .     | 263              | Tennessee . . . . .      | 443              |
| Maine . . . . .         | 593              | Texas . . . . .          | 5,843            |
| Maryland . . . . .      | 383              | Utah . . . . .           | 133              |
| Massachusetts . . . . . | 14,843           | Vermont . . . . .        | 123              |
| Michigan . . . . .      | 8,693            | Virginia . . . . .       | 1,343            |
| Minnesota . . . . .     | 4,343            | Washington . . . . .     | 743              |
| Mississippi . . . . .   | 323              | West Virginia . . . . .  | 383              |
| Missouri . . . . .      | 6,893            | Wisconsin . . . . .      | 5,843            |
| Montana . . . . .       | 233              | Wyoming . . . . .        | 43               |

mately \$100 of its net revenue as a payment to the state for the privilege of doing business as a part of a nation-wide chain. If the tax is to have much effect upon the stores composing the Woolworth system this tax must constitute a considerable part of the previously existing net profits.

The data on Woolworth Company profits, when related to the foregoing figures of the chain-tax impost, are suggestive of an answer to the question of effectiveness of such levies. In 1929, the year which is popularly acclaimed as the best since the World

War, the average Woolworth store made net profits of some \$14,748. In 1932, the worst year in the company's recent history, the lowest net profit, a sum of \$9,051 per store, was realized. Considering now the average tax in relation to the average profit per store the result suggests strongly that the company will not be in any immediate danger of bankruptcy as a consequence of such taxes. In the worst year the average profit realized by each store amounted to approximately ninety-four times the amount of the tax—or, in percentage terms, the tax would reduce net profits of each store by approximately 1.06 per cent, and this in the worst year of the depression. In 1929 the average profits, as indicated above, were \$14,748 per store. On this basis, and in such a year, the net gain of each outlet would have been reduced by less than 1 per cent, specifically by 0.65 of 1 per cent. This is so slight a burden as to indicate, apparently, that these taxes will not bear much weight in determining the success or failure of the Woolworth organization.

It can be conservatively said, on the basis of the foregoing case, that a statute such as the Indiana chain-store tax would have little or no effect upon a chain similar to the Woolworth organization, even though imposed on a nation-wide basis by each of the forty-eight states. It would, therefore, exert almost no regulatory pressure. It should be further noted, in justification of this conclusion, that the assumption has been rigorously adhered to that the full burden of this tax must fall upon the chain. With this assumption withdrawn or modified to take cognizance of the possibility that a part of the burden may be passed on to consumers or back to manufacturers and wholesalers, further strength is given to the conclusion.

#### CASE II

As a chain representing the other side of the picture, the Kroger Grocery and Baking Company may be analyzed in precisely the same fashion as was the Woolworth system. It is possible that a considerably different conclusion will be obtained when this is done. The Indiana taxing bill, because it is representative, will be again utilized.

It will be necessary to indicate the distribution of the stores of

this chain just as was done with those of the other system on a state-to-state basis. From this material in Table 7 the ultimate tax burden of the Kroger Grocery and Baking Company may then be computed.

Not so widely diffused as the Woolworth organization, the Kroger Grocery and Baking Company is more vulnerable to the progressive chain-store taxes, with as many as one thousand stores located in a single state. Presupposing again the existence of the Indiana law on a nation-wide basis, the following tax

TABLE 7\*  
DISTRIBUTION OF KROGER COMPANY STORES

| State            | Number of Stores | State               | Number of Stores |
|------------------|------------------|---------------------|------------------|
| Arkansas.....    | 90               | Missouri.....       | 444              |
| Illinois.....    | 615              | North Carolina..... | 5                |
| Indiana.....     | 360              | Ohio.....           | 1,086            |
| Iowa.....        | 3                | Oklahoma.....       | 5                |
| Kansas.....      | 50               | Pennsylvania.....   | 162              |
| Kentucky.....    | 224              | South Dakota.....   | 132              |
| Michigan.....    | 751              | Virginia.....       | 62               |
| Minnesota.....   | 1                | West Virginia.....  | 102              |
| Mississippi..... | 33               | Wisconsin.....      | 128              |

\* Source: Moody's and Poor's *Manuals* for various years.

burdens, as shown in Table 8, would accrue to the Kroger Company throughout the states in which it is located.

This indicates the amount of the total tax bill which the Kroger Grocery and Baking Company would have been required to pay in each of the states in which it operated. In one state, Ohio, the Kroger Company would have been confronted with a tax levy nearly equal to the total amount imposed upon the Woolworth organization by all forty-eight states combined. The total Woolworth tax bill, it will be recalled, amounted to only \$178,674, while the Kroger levy in the single state of Ohio amounts to \$160,493.

The total imposition by Ohio, Illinois, and Michigan amounts to a figure twice as large as the complete tax burden of the Woolworth Company in all states. The moral to be learned in this connection is this: under legislation of the Indiana type, a chain may

expand to great size extensively without subjecting itself to a heavy burden of taxes but cannot expand intensively within one or a few states save under sufferance of an excessively high levy.

The Kroger organization would have paid a total tax bill of \$604,264, or an average for each of its 4,253 stores of a little less than \$139 per year. The data on average per-store profits for this chain indicate that the effect of the taxing program would here have been quite different than was the case with the Woolworth Company in the previous example.

TABLE 8  
THE KROGER COMPANY TAX BILL UNDER A NATION-WIDE  
INDIANA CHAIN-STORE TAX

| State            | Amount<br>of Tax | State               | Amount<br>of Tax |
|------------------|------------------|---------------------|------------------|
| Arkansas.....    | \$ 11,093        | Missouri.....       | \$ 64,193        |
| Illinois.....    | 89,843           | North Carolina..... | 43               |
| Indiana.....     | 54,593           | Ohio.....           | 160,493          |
| Iowa.....        | 23               | Oklahoma.....       | 43               |
| Kansas.....      | 5,093            | Pennsylvania.....   | 21,893           |
| Kentucky.....    | 31,193           | South Dakota.....   | 17,393           |
| Michigan.....    | 110,243          | Virginia.....       | 6,893            |
| Minnesota.....   | 3                | West Virginia.....  | 12,893           |
| Mississippi..... | 2,543            | Wisconsin.....      | 15,793           |

For Kroger the 1929 data on net profit per store shows a figure of \$946, with a decline during the following recession period to a low in 1932 of \$347. The average store tax levy of \$139 would, in terms of the 1932 experience of this chain, eat up a little more than 40 per cent of the net profits and might, in contrast to the situation in the first case, throw a number of marginal stores from the profit to the loss column, necessitating the closing of such units.

Further emphasis for this conclusion is afforded by a closer analysis of the position of the Kroger outlets. They were heavily concentrated in a few states and would consequently be forced to pay much higher per-store taxes in such districts than in others. Thus in Ohio, where the Kroger Company would have paid \$160,493 as a chain-tax bill, the average assessment per outlet would amount to \$147.78, a sizeable portion of the total store



revenues. In Michigan, with 751 stores, the average tax per unit would amount to \$146.80 and in Illinois, with 615 stores, to \$146.09. The highest figure of per-store levies for the Woolworth Company amounted to an average of \$138.63 in New York state. This figure is considerably below the Kroger level. For the Kroger Grocery and Baking Company marginal stores in Ohio, Michigan, and Illinois would have been hard pressed to justify their existence after payment of these taxes.

The Kroger Grocery and Baking Company in 1935 took in over its counters approximately \$230,000,000 of consumers' money. This compares with a figure of \$270,000,000 for the Woolworth organization. Kroger, on the other hand, would be required to pay a tax bill to the states amounting to three times that of the more profitable chain, doing nearly 25 per cent more business. Still more important is the fact that the Kroger Company operated on a profit margin of only 1.55 per cent, as compared with the 8.38 per cent figure of the Woolworth system in that same year. If the tax bills of the two were adjusted to give each the same burden the impact would be much more severe for the grocery-and-meat chain than for the variety units. When to this is added the fact that the amounts were not the same, that Kroger paid more than three times the tax paid by Woolworth, then the seriousness of this situation is apparent.

One preliminary conclusion is warranted at this point. The bills of the Indiana type, regardless of the rates of progression, are in no way adjusted to the ability of the chains to pay such levies. There is no relation between the number of stores in a chain and the amount of profit, value of the chain privilege, or ability to pay the tax. The Kroger Company, with nearly two and a half times as many stores as the Woolworth Company, transacted only about 80 per cent as much business, made per-store profits amounting to something between 4 and 8 per cent of those realized by the variety chain, and operated on a much smaller margin.

The statute would by no means exert equal pressure upon all chains. The large national chains with stores well distributed between states tend to be much less seriously disturbed by such

taxes than do the local or sectional chains with an appreciable number of stores in each state. It appears, at this stage in the analysis, that the very groups against whom the heaviest punitive pressure was supposedly to be directed are the ones least wounded, while the less hardy, poorly located small chains suffer the greatest hurt.

One objection to the methodology of the foregoing pages may be offered at this point. Reference is made to the fact that the average data on profits per store as given above is the data of actual profits as reported by the chains. From such figures have already been deducted the chain-store taxes paid by each reporting chain. This tends to introduce a certain amount of distortion to the profit reports used in the analysis and the criticism is a valid one.

The results obtained have the effect of showing the pressure upon the less advantageously situated chains as somewhat heavier than it really is and a contrary result appears in connection with the larger national chains. The skew is slight, however, and will not invalidate the general conclusions reached. The more severe measures have been enacted since 1932, and for that reason the period between 1929 and 1932 was selected. Had a later date been taken the distortion would have been greater. As it is the margin of error in the foregoing figures is much less than it would be had the profit reports of today been taken.

This concludes the analysis, in so far as the Indiana type of chain-store-taxing statute is concerned. This is, of course, the most common type, being found in all save one of the taxing states.<sup>2</sup>

The examples used have been introduced to provide a means of estimating through an inductive approach the effects of such legislation upon, first, the large national chains, and second, the local or sectional chains confined to one or a few states. The conclusions speak for themselves.

<sup>2</sup> Reference is made to the Louisiana statute of 1934. The Virginia and Tennessee bills are based on quite different principles and there seems little likelihood of their adoption elsewhere.

## CASE III

The second pattern of chain-tax legislation is now to be considered. The Louisiana statute, upheld in 1937 by the United States Supreme Court is at present confined solely to the state in which it originated but may well spread in the coming years and present serious difficulties for some of the corporate-chain groups.

The provisions of this Louisiana statute will now be presented, in Table 9, before the analysis goes farther.

This statute, it must be remembered, imposes a tax upon each store within the taxing state, the tax to be computed in terms of

TABLE 9\*  
TAXING PROVISIONS OF THE LOUISIANA STATUTE

| Number of Stores<br>Wherever<br>Located | Tax Rate for<br>Each Store<br>in State | Number of Stores<br>Wherever<br>Located | Tax Rate for<br>Each Store<br>in State |
|-----------------------------------------|----------------------------------------|-----------------------------------------|----------------------------------------|
| 1- 10.....                              | \$ 10                                  | 176-200.....                            | \$200                                  |
| 11- 35.....                             | 15                                     | 201-225.....                            | 250                                    |
| 36- 50.....                             | 20                                     | 226-250.....                            | 300                                    |
| 51- 75.....                             | 25                                     | 251-275.....                            | 350                                    |
| 76-100.....                             | 30                                     | 276-300.....                            | 400                                    |
| 101-125.....                            | 50                                     | 301-400.....                            | 450                                    |
| 126-150.....                            | 100                                    | 401-500.....                            | 500                                    |
| 151-175.....                            | 150                                    | Over 500.....                           | 550                                    |

\* Source: *Acts of Louisiana*, 1934, No. 51.

the total number of stores in the chain, wherever located. If the act is assumed to be in operation in all of the states, as was done in the examples used to illustrate the effect of the Indiana-type bill, it matters little where the various stores of the chain are located, whether in one state or many. If each of the forty-eight states imposed such a tax as the Louisiana measure, then the tax bill for any chain having more than five hundred outlets would be an average assessment of \$550 per store. If this act were applied to several of the chains already discussed, some comparison between the size of the tax burden for different classes of chains would be evident. The method used in computing tax burdens under this act is relatively simple. The total number of stores owned by the chain must be obtained. This figure is then multiplied by the tax rate effective at that level and the total tax is

then determined. The data in Table 10 give the total tax bill for several of the chains under these assumptions.

These figures make it quite apparent as to why the Great Atlantic and Pacific Tea Company so hotly contested the constitutionality of the Louisiana chain-store tax. Taking almost three-fifths of the company's profits, there is considerable likelihood that such a statute would force the closing of several stores.

For each of the ten nationally known chains listed above, some change is effected. In the case of some, such as the Safeway Stores

TABLE 10  
CHAIN-TAX BILLS UNDER A NATION-WIDE LOUISIANA-TYPE STATUTE

| Chain                                     | Total Tax   | Net Income of Chain (1935) |
|-------------------------------------------|-------------|----------------------------|
| F. W. Woolworth Company.....              | \$1,089,000 | \$31,247,000               |
| S. S. Kresge Company.....                 | 409,750     | 12,247,000                 |
| S. H. Kress Company.....                  | 70,200      | .....                      |
| W. T. Grant Company.....                  | 232,500     | 3,334,000                  |
| J. C. Penney Company.....                 | 814,550     | 15,373,000                 |
| National Tea Stores.....                  | 684,750     | 1,585,000                  |
| Kroger Grocery and Baking Company.....    | 2,357,300   | 4,111,000                  |
| First National Stores.....                | 1,459,150   | 3,457,000                  |
| Great Atlantic and Pacific Tea Company... | 8,484,000   | 13,984,000*                |
| Safeway Stores, Inc.....                  | 1,775,400   | 1,481,000                  |

\* Income for 1933.

organization, the imposition of such a tax would establish a burden heavier than the total net profits of the chain and would force the system out of existence in rather short order, unless it were drastically reduced in size. In the case of others, such as the Woolworth chain, the tax comprises only some 3-4 per cent of net income and would effect no drastic changes in the scale of operations of the company.

Since one of the professed purposes of such legislation is the control of bigness in the merchandising field, the Louisiana tax should be evaluated in terms of possible attainment of such a goal. If bigness is used to mean the existence of many units controlled from one central place, then the Louisiana type of taxing statute appears to come close to achieving its goal. At any rate, it more nearly attains such a position than does the Indiana type.



The latter was found to penalize small chains heavily if they were confined, as most small chains are, to a single or a few states. On the other hand, large chains, if well scattered throughout the country, escape with a comparatively light burden. Under the Louisiana type of tax a chain with more units will always pay more than one with a few regardless of the distribution of its outlets between states. The Louisiana statute appears to be more acceptable if bigness is defined in terms of the number of outlets controlled centrally. If, however, that word is defined to cover such vital matters as the size of the sales volume, number of employees, amount of invested capital, and profitability of operations then there still appears to be something wanting even under the Louisiana form.

## CHAPTER V

### THE INCIDENCE OF CHAIN-STORE TAXATION

**B**EFORE any final statement can be given as to the effects of the chain-store taxes some consideration must be given to their impact upon groups other than the corporate chains. The position of those who buy from the corporate systems must be analyzed. Such a group embraces but a small portion of the consuming public, however, and it seems probable that those who purchase from other retailing entities will also be affected, directly or indirectly. The customers of the independent merchants, super-markets, and co-operative chains likewise have an interest in this affair.

So much for the consuming public. Other groups will also be influenced by this legislation, and here belong the many manufacturers and middlemen who sell to the corporate chains. It may be that the chains will attempt to shift the burden of these taxes forward to the consumers and backward to the producers. In either event both groups become interested parties. The position of the consumer will first be analyzed.

#### CHAIN STORES, CONSUMERS, AND CHAIN-STORE TAXES

The foregoing analysis defines the problem to be considered in the following pages. Will the chains be able to pass their tax burden on to the public, or must they assume it as best they can? It is generally believed that these taxes, because they are imposed upon the gross rather than the net incomes of the chains, may be shifted. The problem is not so simple, however, and the answer to this question will rest upon a number of factors, some almost completely indeterminate, others possible of crude solution—none, perhaps, susceptible to precise conclusions. Among these factors are the following: the degree to which competitive or monopoly conditions are found, the nature of the cost situation



and  $Y$ , the quantity sold by him must drop under the assumptions to zero. Perfect elasticity is noted. If, on the other hand, his price is lowered to some point below  $X$ , then the quantity sold at that level,  $Z$ , becomes infinite, with limits set only by the capacity of the retailer to supply the market. This is shown as quantity  $O-B$ , the limit of the stock held available.

If competition were perfect between all retailers, and if, as would follow, the prices of all were identical, then it would be true that no chain store could pass even so much as the smallest portion of these taxes to the consumer. This would be exactly opposite to the popular belief.

The situation would be similar to that shown in Figure 1, where the smallest increment added to price forces the quantity sold to zero, unless all dealers in the market make the same addition. Under such perfectly competitive conditions an effort to add the burden of these taxes to the selling price would meet with failure. There would, of necessity, be some decline in profit margins at the chain store.

It is now time, however, to withdraw certain of these assumptions. The situation is far removed from perfect competition, and one step may be taken toward reality at this time. Let it now be assumed that within the retailing field there are certain distinct classes of dealers, each class being isolated within itself. There is little or no competition between these classes, but within each class competition is keen. Let one class be known as the independent merchants and the other as the chain dealers. Competition between chains is perfect; competition between independents is perfect; competition between chains and independents is non-existent. Competition is confined solely to a price basis, and there is a spread of 10 per cent between chain and independent prices. These are the assumptions which will be drawn at this point. These changes have removed the earlier assumption of perfect competition throughout the retailing field. An element of imperfection has been introduced with the assumption that no competition exists between the classes.

Let Figure 2 represent this situation. Here  $OC$  is the level of prices charged by the chain stores and  $OI$  is the level of prices



established by the independent merchants.  $IC$ , the difference between the two, equals one-tenth  $OC$ . The position of both independent and chain dealers is similar to that indicated in Figure 1. No chain merchant can raise his prices in the slightest degree without losing his entire volume of business to his competitors, the other chain merchants. Each independent dealer is in the same position. (While an independent merchant might on occasion consider the possibility of reducing his prices and thereby unloading his entire inventory, such a contingency may be ig-

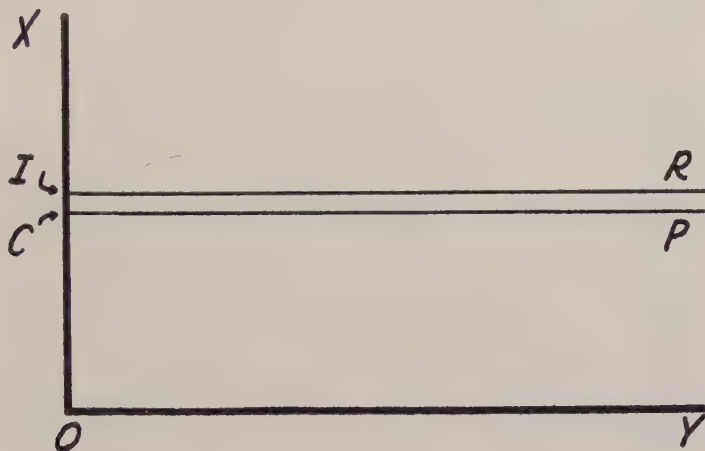


FIG. 2

nored, since an individual proprietor would constitute an infinitesimal factor by himself and his actions would have no influence upon the entire situation.)

Now let one additional assumption be drawn at this point. Let a tax be imposed upon chain stores which adds equally to the burden of each. Let the amount of the tax be equivalent to a 3 per cent increase in the costs of doing business. This will be a marginal tax which will bear evenly upon all of the chain dealers. All will feel a similar pressure to increase selling prices by an amount sufficient to cover this increased cost. Let this situation be portrayed in Figure 3. Whether all shift together or a scattered few take the initiative in this move is a matter of almost complete indifference, in so far as the conclusion is concerned. If

a few take the lead they may for the moment lose trade to their rivals who hesitate to increase their selling prices. The tardy dealers will tend to sell their full inventories, but will do so at a reduced margin of profit. As this condition develops, however, they will increase their prices to offset the declining profit margin and ultimately will be selling at an amount sufficient to restore their former profit margins. This level will be exactly that of the other chains.

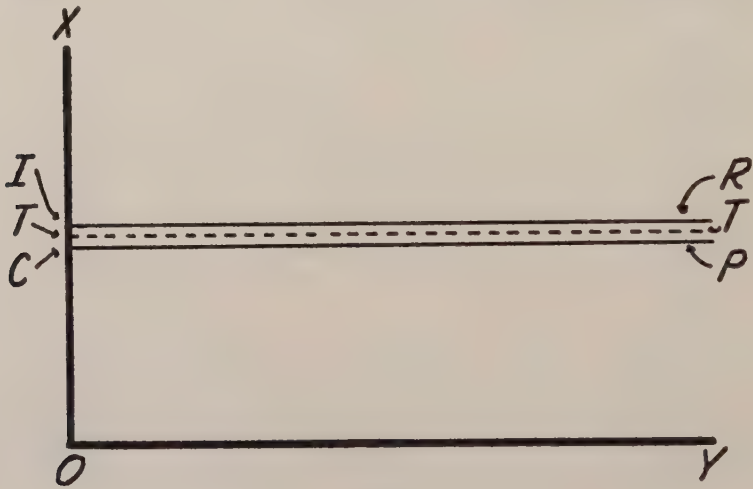


FIG. 3

Referring now to Figure 3:  $OC$  is the level of chain prices before the imposition of the tax;  $OI$  is the level of independent prices, with the difference  $CI$  representing the 10 per cent spread between the prices of the two classes;  $CT$  represents the 3 per cent burden of chain-store taxes; and  $OT$  represents the new level of chain-store prices after the tax has been levied and the chains have all made their adjustment to the added burden.

This increase in chain prices will not be sufficiently large to carry the chains over into the independent market. Thus, with only the two classes, and with competition restricted to a price basis, there can be no limitations upon the power of the chains to shift the burden of these taxes to their customers. This group will still prefer to deal with the chain, for reasons which have in the

past prompted their trading habits, and the reduction of the price differential from 10 to slightly more than 7 per cent will not alter the arrangement.

It is now time to consider the removal of another of the assumptions which has been carried to this point. It has been held, until now, that competition between these two classes was confined to a price rivalry. Such, of course, is not the case. Competition is based also upon service features. These may be divided into two type distinctions—product differences and environmental differences. The first has to do with the article itself, the second with the services which attend the sale of the article.

Product differentiation, the first of these two types, may involve many factors. It may be attributed to actual differences in the quality or quantity or it may be due to less tangible factors, such as trade-marks or individual brands.

Environmental differentiation may be equally profuse. Differences may be represented by such highly intangible factors as the personality of the dealer, terms of sale, store atmosphere, and the like. There are a number of other distinctions which belong in the middle ground, bearing characteristics of both product and environmental differentiation. Such a factor would be represented by the packaging of the product. In so far as the consumer is concerned, this may be said to create a mental difference in the product itself. On the other hand, it appears equally representative of a class of environmental distinctions. The package is but a part of the environment surrounding the product.

Up to this point the influence of such factors was reduced to a negligible position by assumptions which were highly unreal. The effect obtained when they are introduced to the analysis will be noted now, although the detailed analysis of their effects will properly be left to a later page.

If competition is assumed to involve something more than price influences alone there will be a much greater overlapping of market areas than was assumed previously. Consumer decisions to trade at chain or independent stores represent a nice adjustment of price and service factors, together. Anything which adds to or detracts from either of them will bring about a shift in con-

sumer habits, a readjustment of markets. The problem becomes one of indifference relations. There must, in a real world, be many who are just at that margin of indifference where the combination of price and service features offered by both chain and independent are so nearly equal that it makes little difference with which group they trade. Price advantages to be found at the chain outlet are balanced by service offerings of the independent unit. And, to repeat the statement given above, anything which adds to or detracts from either price or service features of any dealer or group of dealers must bring about a readjustment of markets in line with that change.

When the price advantage of the chain store is reduced by higher selling prices, introduced to offset the chain-store tax, then the balance, for those in a position of indifference at least, must swing in the direction of the independent. This will suggest a provisional limitation upon the ability of the chains to pass such taxes on to the consumers.

It is time also to withdraw another of the assumptions made above. It has been previously held that there were only two classes in the distributing picture—the chains as one completely homogeneous group and the independents as the other. This position may now be altered by introducing a third class, whose position will be midway between that of these two groups.

Let the co-operative chains, groups of affiliated independents, be introduced to the scene. Let the 10 per cent differential which formerly existed between chains and independents remain, but let the co-operative chains assume a midway position, with prices 5 per cent above those of the corporate chains. Let it be further given that competition is based partially upon price, partially upon service factors. With these conditions inserted into the foregoing analogy, further limitations appear as to the ability of the burdened chains to shift the incidence of the tax onward to its customers. There are now three rather than two classes in the picture. They compete but little on a price basis, perhaps, but customers of all three have adjusted their purchasing habits to fit in with what they understand to be a proper weighting of price and service features combined.



While the tax might be shifted completely if there were no service elements in the competition and only price factors (there is a five-point spread between the prices at the chain stores and those established by the nearest price competitor, the co-operative chain, while the tax was assumed to be only a three-point impost), the existence of these service features precludes any such complete readjustment as this. In the graphical portrayal of this situation in Figure 4, column 1 represents the assumed relative

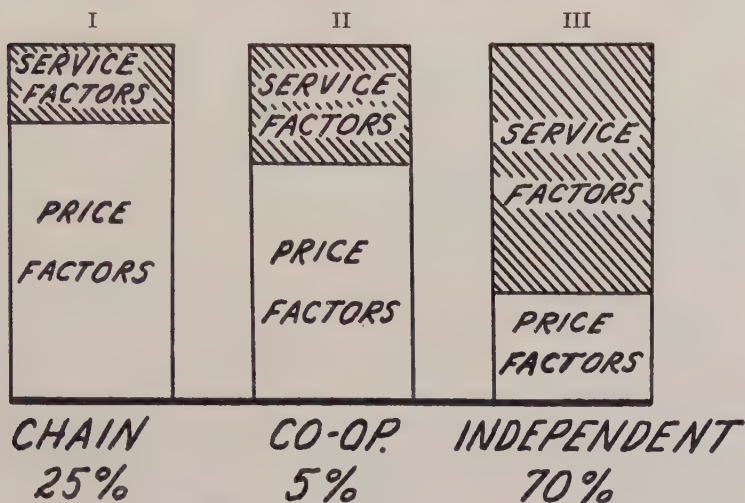


FIG. 4

importance attached by patrons of the chain stores to the two factors of price and service; column 2 represents the respective importance of service and price features in the case of co-operative-chain patrons; column 3 represents the same element in the case of the independent dealers. The share of each class in the total of the nation's retail business is indicated by the figures at the base of each column. This distribution is assumed to be momentarily frozen, with the corporate chains transacting 25 per cent of the country's retail business, the co-operative chains 5 per cent, and the independent merchants taking the remaining 70 per cent. For the moment there is an equilibrium at this position.

Price factors are most important to the patrons of the corporate

chains, they are least important to the customers of the independent stores, who count service features more heavily. Among co-operative-chain customers price factors count for less than they do with the corporate-chain group, but more than with the individuals who purchase from the independent stores. The co-operative chains, therefore, occupy a midway position with regard to both factors.

The equilibrium established at this moment is only a temporary affair, and any factor which will effect a change in either price or service aspects for any of the three groups will disrupt the situation. Such a factor may be found in these chain-store taxes. If the corporate chains seek to pass the burden of taxes on to the consumers, this will tend to force a readjustment of consumer purchases, so that the percentage figures of chain participation in total sales (as given at the base of column 1) must decline, and one or both of the other groups must gain. This will be so because the value of the price factor as a device for attracting customer patronage will vary inversely with the price itself, decreasing in importance when chain prices rise relative to those found in the other two classes. Unless the chains can increase the importance of service factors to offset this situation such a decline must follow.

The introduction of this third group, the co-operative chains, illustrates the effect of narrowing ranges as between noncompetitive zones. As more and more classes are introduced to the scene the intensity of competition between them must make price changes by any one class more difficult.

During the course of the analyses already made it has been rigidly assumed that competition was keen within groups, but stolid as between groups. It was held that each chain within the corporate class would be forced to align itself with the group, that price differentials could not exist between chains because of the high order of competition within the class. Now a further stride is to be taken in the direction of reality with the breakdown of this assumption. It has been held that all members of a given group were identical, that each chain had its counterpart in the others. Obviously, this is not a valid condition for an analysis which hopes to approach the actual experience of the groups involved.

It will now be understood that there are points of differentiation within the chain group—that some chains operate at a higher level of costs than do others, that all do not sell at identical prices, and that there are differences in the service offerings of the various systems. In Figure 5 let it be assumed that there are two distinct types of chains; that at the present moment both are selling at identical prices; that one is experiencing a higher cost of operations than the other; and, finally, that the burden of chain

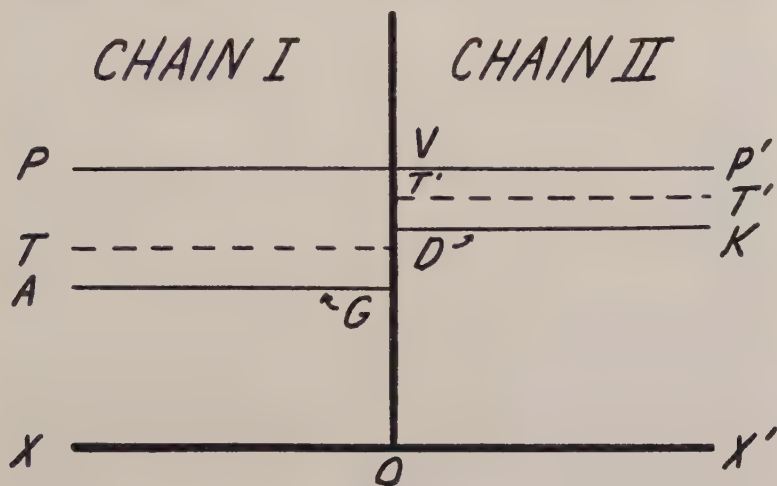


FIG. 5

taxes will be identical for both. Let  $AC$  be the curve defining the average total unit cost level of Chain I at a given stage of operations. Let  $DK$  be the curve denoting the similar cost level of Chain II. Let  $PVP'$  be the curve which indicates the price level common to both. Let  $TT$  and  $T'T'$  denote the tax burden born by Chains I and II, respectively. Let the quantity sold by each and the conditions of demand confronting each be disregarded for the moment. Let the problem be this: to consider the extent to which either or both may shift the burden of their tax levies to their customers. On a price basis there is nothing to distinguish one chain from the other; both are selling at a price of  $OV$ . Chain I is handling its normal sales volume at an average unit cost of  $OC$ , whereas Chain II is transacting business at a cost of  $OD$ . As

in the former case, it is here assumed that the patrons of all corporate chains have adjusted their purchasing habits to the evaluation which they have placed upon both price and service offerings of all chains in Class I and all chains in Class II. Any factor which negatively influences either the price or service arrangements of the chains in one of these classes must turn consumer trade from it to the other. It is assumed, as noted, that the tax burden falls evenly upon both classes.

Under these conditions the costs of chains in Class I must rise from  $OC$  to  $OT$  and for chains in Class II costs will rise by the same amount from  $OD$  to  $OT'$ . The margin of profit for chains in Class I declines from  $VC$  to  $VT$  and for those in Class II it falls from  $VD$  to  $VT'$ . It is apparent that considerable pressure has been brought to bear upon the second group, which may now be tempted to raise selling prices in order to offset the declining profit margin. This cannot be done, however, without losing customers to chains in the first group, unless of course chains in Class I decide also to raise their prices by the same amount.

Will they be apt to do so? While the answer to this question is somewhat indeterminate, it seems probable that such will not be the case. Although, in terms of the assumptions made, perfect competition has been eliminated from the picture, it must be admitted that neither of these chains will completely ignore the effect of its actions upon those of competitors.

If chains in Class I consider the possibility of raising their prices they will, of course, recognize the fact that such a possibility is then available to chains in the other group. While both will have tended to offset the burden of these taxes, both will not have gained equally by the establishment of this higher level of prices. Chains in Class I found their profits diminished by the tax, let us say, to about 25 per cent, while those in Class II, because of the smaller margin upon which they have been operating, saw profits cut in half. A 25 per cent loss has been experienced by one, a 50 per cent loss by the other. It is from this point that an analysis of the probable actions of each must begin.

If it be assumed that Class II chains were operating on a profit margin of \$2.00 per \$100 of sales and those in the other group



were obtaining a return of \$4.00 on each \$100 of merchandise sold, then the tax in line with the foregoing would have been the equivalent of \$1.00 for each. Such a levy cuts the profits of Class II chains by 50 per cent, leaving a net of but \$1.00. This same amount of tax cuts the profits of Class I chains by but 25 per cent, leaving a \$3.00 profit.

If at this point Class I chains decide to raise prices by an amount sufficient to restore the former level, they will be increasing profits from the post-tax level by but  $33\frac{1}{3}$  per cent. Their line of action will have made it possible for Class II chains to raise their prices by the same amount and this will increase their post-tax profit margin by 100 per cent. Both, because of their higher prices, will lose some trade to independent merchants and other untaxed retailers. It seems evident that Class I chains would not be apt to inaugurate a line of action which would be considerably more beneficial to the other chains, and the possibility of Class I chains doing so can now be dismissed.

On the other hand, if Class I chains do not raise their prices, those in the other group are faced with two unpleasant alternatives. Either they may continue to sell at the previous level of prices and receive drastically reduced net revenues or, as the other choice, they may decide to raise prices to compensate for the cost increase. If the latter possibility is accepted trade will be diverted to Class I chains, which will gain thereby. Thus the tax levy will raise the costs of doing business. Any attempt to offset that added cost must result in a decline in the volume of business transacted.

Whether Class I chains will find the increased volume of business on a smaller unit profit sufficient to offset the decline in per-unit income caused by the taxes is problematical. It seems almost certain that the tax burden will become less obnoxious, however, as it is spread over this increased volume of sales.

If Class II chains decide to continue selling at the prices set by the other group there will be a consequent decline in revenue and, over a period of time, a shift of invested funds from the chains in Class II. This investment may be transferred to chains in the

other position or may be diverted to other entities in the retailing field, or removed from that field entirely.

There appears, consequently, to be little likelihood that the chains which find these tax levies least burdensome will take the initiative in shifting the levy to the consumers. And if other chains, feeling the burden more heavily, attempt to shift their taxes, they will be able to do so only at a sacrifice of some portion of their business. This diverted trade will turn to the co-operative chains, to the super-markets, and to the independents, as well as to other corporate chains which make little effort to shift their taxes.

#### LAND, LABOR, AND CAPITAL AND THE CHAIN-STORE TAXES

If the possibility of shifting these taxes forward to the consumer or backward to the producer was slight in any instance, another group of possibilities present themselves.

To the extent that chain wages are above the minima set by the various wage-and-hour laws, and to the extent that union activity does not make such a course impossible, these taxes may be shifted backward in another cost-reducing effort by decreases in the pay roll. Presumably, if there were no union standards and if wages stood above the legal minimum, there would be few limiting forces which would prevent an appreciable escape from the tax burden at the expense of labor.

Another possibility may be suggested. If the tax is assumed by the chain the burden will be carried by capital. If it is passed back in the form of lower wages labor will assume a portion. There is also some likelihood that realty holders, the land interests, will have a share to bear. New leases may be signed by the chains only at reduced rentals. In a period when the realty market is not strong there may be no alternative for the real-property holder. There is a possibility that each of these groups will be required to assist the chains in bearing the burden of these taxes.

The fact should not be overlooked that the recent chain policy of closing weak and inefficient units and thereby reducing costs is

also another means of shifting a part of the burden to others. To the extent that this reduces wages and rentals received from the corporate chains it is but another, and a less apparent, means of passing the final incidence to groups other than those upon whom the levy was initially imposed.

In this connection the following data are interesting. *Barron's*<sup>2</sup> reports that labor, farm, real estate, and consumer groups all went on record as being opposed to chain-store taxation.

The American Federation of Labor at its annual meeting in October, 1938, adopted a resolution commending the chain store and condemning chain-store-tax legislation. Presumably this was not done in a spirit of public beneficence.

In November, 1938, the American Farm Bureau Federation, in its annual meeting, condemned discriminatory and punitive taxes as increasing costs to consumers, reducing consumption, and limiting production in agriculture as well as industry. The National Grange adopted a like resolution at its meeting in the same month.

The National Association of Real Estate Boards, at its annual convention in October, 1938, passed a resolution praising the chain stores extravagantly and likewise condemning chain-store taxation for its effect on real estate values and general business recovery.

#### CONCLUSION

Chain-store taxes will be borne by labor groups to the extent that they are unprotected by labor organizations and are receiving wages above the minima set by state and federal laws. The taxes will also be shifted to some producers who are not protected by the Federal Trade Commission and the Robinson-Patman Act. Real estate owners must also expect to assume a part of the burden, either in the form of lower rentals per store or fewer stores per chain. Capital, as represented by the stockholders of the corporate chains, will bear the amount of the taxes which is

<sup>2</sup> February 27, 1939, p. 5.

assumed by the chains after all possible efforts to offset the burden have been made.

Indirectly, all of these groups may be thought of as consumers, and it might be said that the tax will ultimately be borne in its entirety by the consumers. This will, of course, be true only in this limited sense of the words. It appears doubtful whether the chains will find it advisable, and in some instances even possible, to attempt a direct forward shift of the burden to their customers.



## CHAPTER VI

### GOVERNMENT AND THE CHAIN STORES

#### AN APPRAISAL

THE preceding chapters have presented and analyzed the many attempts of state, local, and federal governments to provide for the regulation of the corporate chains. This survey has embraced a considerable body of legislation designed to control the activities of such merchandising systems. Nearly all of this regulatory program has come into being during the short span of one decade.

Some measures have been introduced only after intensive investigation of conditions within the chain-store field. This, however, with a few exceptions, has been true only of federal legislation. State and local law-making bodies have first enacted, and then considered the effects of, their edicts. It would be more surprising than otherwise if many parts of this program were not at odds with other sections. In this chapter an attempt will be made to evaluate the entire program, although the primary emphasis will incline toward the tax programs of the state governments.

Over fifty chain-taxing statutes have been passed by the states, and at least that many by municipal bodies. More than forty fair-trade-practice laws have been directed at the corporate chains, and at least two by the federal government, while countless others have been or are being considered today. None of these measures have been introduced to assist the chains, and many have been enacted with the specific intent of seriously injuring them. All have had some effect, too frequently not that intended by their sponsors. In most instances the full impact of such legislation is not understood and probably will not be realized for many years. All of this serves to indicate something of the overwhelming difficulties which block any effort to fairly evaluate such programs. At best only a few of the more evident results can be offered. Some of them will be open to question, others are more definite.

By and large, state legislators have shown surprising tendencies to completely ignore the very nature of chain-store operations during the evolutionary stages of their regulatory programs. This fact throws a serious question either upon the competency or the intentions of such bodies. Failure to seek an understanding of the functional mechanics of any groups which are to be regulated casts an aura of incompetence around the would-be regulators.

Only two explanations for the course which state regulation of the chains has taken appear possible. If the state legislatures have understood the nature of the entities they were regulating, then their actions are not those which might be presumed to logically follow such understanding. If this is the case, then the intent of the legislators can be branded as something quite different from that expressed. If, as the other alternative, they have failed to acquire a knowledge of the operations of chain systems, then their actions must be branded as wantonly neglectful of the high requirements of diligence which should be expected in public office.

In any case, the statutes enacted by state legislators fail miserably to accomplish either the purposes expressed by the legislators or any other reasonable goal which might be expected to exist. The passage of chain-store-taxing statutes can be explained only on political grounds. Economic or social factors are far in the background, dominated by factors of political strategy. However, the motives which prompt such legislation are of little concern where the issue has to do with the effects and not the explanations of such legislation.

Plunging directly into the critique, it can be initially stated that chain-store-taxing legislation, itself, offers no palliative for whatever evils may arise out of the corporate-chain systems.

It has been frequently said that the chain organizations, by their size alone, constitute an undesirable element in the retailing field. It is now time to offer a final word on this point, since it seems destined to play no small part in future efforts to regulate the chains.

No such philosophy was accepted one decade ago by any save a small minority. The emphasis was all in the other direction. Among men in public life only a few appear to have taken this

viewpoint consistently. Mr. Justice Brandeis was one of these, and his dissenting opinion in the Quaker City Cab Company case in 1928<sup>1</sup> amply illustrates the tenacity with which he has clung to the position that size, even in the absence of other malignant forces, is undesirable because of the power with which it is necessarily accompanied.

There are approximately 140,000 retail chain units in the country. These are owned by approximately 5,500 individuals and corporations. This places an average of slightly over 25 stores under a single jurisdiction. However, the actual distribution is more in point than any average figures. The great majority of the corporate chains are small local affairs. Only 84 chain organizations operate as many as 100 units but these 84 systems have 48,000 outlets under their control. This represents one-third of the total number of chain stores under the control of one-sixty-fifth of the chains. More in point, it is found that these larger chains transact slightly more than one-third of all chain business. When to this is added the fact that chain systems as a group constitute only one-tenth of the total number of retail stores of the nation, yet do one-fourth of the retail business, the pyramiding of control becomes more apparent.

In the whole of the United States there are almost 1,500,000 retail dealers and business firms. Of this number 84, or .000056 of 1 per cent, do 8½ per cent of the total nation's business. So much for the matter of strategic position.

There are many who, while aware of the numerous advantages which have generally accrued as a result of chain operation, still feel that the "evils incident to the accelerating absorption of business by corporations far outweigh the benefits thereby secured." They point to the extent of chain dominance in individual fields. Data presented before the Temporary National Economic Committee by Willard L. Thorp illustrates this point: "In 1935 the chain form did 91 per cent of the variety store business, 38 per cent of the grocery store business, 29 per cent of the busi-

<sup>1</sup> Cited above, chap. iii, p. 31, n. 2.

ness in drug stores with fountains, and 14½ per cent of the business of restaurants and eating places.''<sup>2</sup>

The social and economic effects of this concentration have been told and need not be repeated here. It will be in point, however, to indicate that chain-taxing legislation as generally developed by state legislatures offers little ground for expecting any diminution in size. In a previous chapter it was shown that size as measured by the number of stores in a chain had little meaning. Other connotations of more significance were suggested. Among these were: the number of employees, sales volume, capital investment, and strategy in position. In scattered instances these taxes have driven a few chains out of the field. More, however, have withstood the impact of this legislation and several have actually increased in size as measured by these latter standards. Some have decreased the number of stores under their control while appreciably increasing the volume of business done by each remaining unit. Some which were most in need of control have largely escaped. The Indiana type of legislation punishes the regional and local chains, but bears less heavily upon nation-wide organizations. The Louisiana type measures chain size solely in terms of the number of stores and heavily punishes a chain having many stores. All of this has occurred in the face of the Federal Trade Commission investigations which conclusively proved that there was no direct relationship between the number of stores and profitability, dominance, or antisocial behavior. Some of the chains which rank among the largest from the standpoint of capital investment, number of employees, and share in retail business, are not among the largest when measured in terms of the number of stores operated. Such chains escape the burden of these taxes, and it seems from this that chain-tax legislation, as developed down to the present time, must be considered a failure when it comes to curbing organizations of great size.

While it may seem to some that these taxes are aimed at the number of units in the chains, such on the testimony of state

<sup>2</sup> Digest of testimony of Willard L. Thorp before the Temporary National Economic Committee. U.S. Department of Commerce, Bureau of Foreign and Domestic Commerce, *Domestic Commerce Bulletin*, Dec. 10, 1938, p. 342.



legislators is not the case. Taxes directed at the number of units, it is said, were the only means available for accomplishing the real goal, the elimination of unfair competitive practices, large size, and antisocial behavior. It will be well, then, to examine the taxes from this point of view. One of the "unfair" practices against which this legislation was assertedly directed has been the receipt of special discounts and allowances. It is somewhat difficult to understand or realize in just what manner these taxes were supposed to discourage such tendencies. It may have been assumed that the tax levies, and this is quite erroneous, by burdening the chains and forcing a reduction in chain size would likewise reduce bargaining power. In the first case, as indicated in the body of the study, there has been no great decrease in chain size (sales, capital investment, etc.) as a result of these levies. Second, there is little reason for assuming that there would be any real decreases in either the amount or extent of such discounts even though chain groups were forced to operate on a somewhat diminished scale. Their purchases would still be larger than those of independent dealers, and generally larger than those of the co-operative chains. More than this the chains themselves, if burdened by such legislation, would feel even greater pressure to obtain such discounts. If the taxes became burdensome the chains would attempt to reduce their costs of operation, and one apparent method of accomplishing this would be that of obtaining their inventories at reduced prices. The pressure of chain taxes would in fact tend to lead the chains to seek preferential treatment in their own purchases.

Much the same criticism may be offered in connection with these taxes when enacted to discourage or prevent undesirable pricing policies. These taxes are taxes upon the business of chain-store operation, upon the gross income and not the net revenues of the chains. Their impact may be offset by the reduction of other costs, as represented in special discounts and allowances, or by spreading them over a larger volume of sales, thereby reducing the relative burden. One of the most popular chain methods of sales stimulation has been the leader sale. Far from discouraging sales at leader prices the chain-store taxes encourage such devel-

opments as necessary offsets to whatever of punitive nature the chains may find in such legislation. If, as was found to be the case, the chains concentrate their leader selling upon nationally advertised products, then chain-store taxes, by themselves, tend to a more intense exploitation of such items.

One of the most important of all the considerations advanced in support of chain license fees has been that which deals with the competitive situation in the retailing field. It has been alleged that the growth of chain systems of large size has led to the gradual dissolution of competition. This point was fully covered in an earlier chapter, but at this time some consideration may properly be given to the introduction of chain-store taxes as a means of preserving competitive force. It was argued that these taxes by harming the corporate chains would tend to improve the competitive vigor of the independent merchants. Statistics indicate that there has been no regular increase in the independent merchant's share of the nation's business. Nor has any appreciable decrease been experienced by the corporate chains.

There has, however, been one result which was probably not foreseen at the inception of this legislation. The co-operative chains, which began to grow during the late 1920's, became a regularly more important factor in the situation. Whether the tax penalties meted out to the corporate chains did anything to encourage independent merchant participation in these co-operatives is problematical. At any rate, every indication points to a more intensive form of competition in the future, with co-operative chains bringing the independent merchant to a stronger position, with the super-markets and local, sectional, and national chains all entering into keen rivalry for the nation's business. Those independent merchants who have not become affiliated with co-operative associations appear to be dropping farther and farther behind in the race and the tax legislation does not appear to have helped them in the past or offer much hope of assistance in the future. Their salvation appears to lie more logically in the co-operative movement.

One of the assumptions apparently made by those who have enacted these taxing statutes is the supposition that all chains are

alike, if they are of equal size, as measured by the number of outlets under single management. Such a position completely disregards the wide variations as between the different fields entered by the chains. It disregards the fact that in certain lines of activity only a small profit can be garnered by an individual unit, whereas in other fields the individual outlets show high profits. This condition is well illustrated by a comparison of units in the gasoline-filling-station field and those in the variety group. For the latter, store sales and profits are large by any scale. The gasoline stations, on the other hand, are in an exactly dissimilar position. The assumption is quite erroneous.

Such a belief, however, coupled with the further assumption that all other forms of retailing present exactly homogeneous units, led to the passage of chain-taxing statutes as a means of equalizing competition. A given rate of taxes would presumably wound all chains equally and thereby benefit other forms of retail distribution in the same proportion. The equalizing of competitive advantages may well be a worth-while aim of governmental policy. These chain-store taxes scarcely commend themselves for the task.

One of the most serious charges which can be brought against any regulatory program is the statement that it is not needed. There are three fundamental standards which must be established for all regulatory platforms. In the first place, the regulation must be intended to accomplish some necessary purpose. Second, it must be reasonably probable that the program will accomplish that goal. Finally, the program must not, in the course of its development, unreasonably intrude upon or impair other interests. When applying these standards to the state chain-store-taxing legislation a number of interesting conclusions emerge.

The necessity for state regulation of the chain stores will depend upon the nature of chain operations, the other types of regulation affecting these operations, and the success of those other regulatory measures in curbing undesirable chain actions. Unquestionably there have been a number of chain practices which were not justifiable. Loss-leader selling, one of the mightiest of chain weapons, has many antisocial implications. Quantity

discounts were too frequently based upon no real savings, but depended simply upon the amount of pressure which a given chain was able to apply when purchasing from the manufacturer or middleman. This, too, was undesirable. Upon occasion the chains have also been guilty of competitive practices which, mildly stated, were overly ardent. All of these point to the need for some type of regulation in the interests of the general public. It may be seen that the chains, by reason of their own actions, were fit subjects for regulation. The first of the standards noted above appears answered. Control was desirable—was, in fact, necessary.

The second requirement holds that the regulatory device adopted by the state be reasonably expected to accomplish the type of control needed—that it will, in short, discourage or put an end to such practices as have been held undesirable during the investigational phase of the regulatory program. Can chain-store taxation be expected to prevent or discourage loss-leader selling, excessive quantity discounts, or other unfair competitive practices? Can it be expected to bring about a reduction in objectionable size? The answer has already been given. Objectionable size is not necessarily that found in chains having a large number of units, yet this is the sole standard of measuring size adopted by these tax-control bills. The taxes are inadequate if enacted as measures to control undesirable size within the corporate chains. There is, furthermore, little room for assuming that anything in these taxes will discourage the use of loss leaders, the acceptance of quantity discounts, or the employment of other undesirable trade practices. Indeed, there is some ground for believing that they will have precisely the opposite effect, tending to encourage rather than discourage such actions. Most important, however, is the fact that the state and federal governments have already adopted measures intended to specifically control certain of these undesirable developments and with such legislation in force the need for chain-store taxes seems nonexistent.

The efficiency with which the chains have handled their problems in the past marks them for special consideration. They have demonstrated their value to the public on a price, product, and service basis. That there have been undesirable aspects to this



development goes without saying, but it appears impossible to draw up such a list of these undesirable practices as would warrant the complete destruction of the chain system of merchandising. The chains have proved their value to society. Any attempts to regulate or curb the operations of such entities must accordingly demonstrate the fact that society will be in a better position after the enactment of these taxes than it will before. The burden of proof should rest (although legally it does not) with the states and they have not as yet proved their case.

The foregoing discussion has been concerned primarily with the regulatory aspects of chain-store taxation. Taxes are normally, however, enacted as revenue, not regulatory, measures. Some effort has, accordingly, been expended to justify the chain-store taxes as revenue bills and this point may now be considered. The validity of such a claim is immediately subject to doubt when it is discovered that the chain-store taxes have produced little revenue, have added little to state coffers. If they have been passed as revenue measures they have dropped far below expectations, so far short that there is every reason for assuming that the revenue explanation was never more than an excuse for such statutes.

In line with this approach it has been suggested that the chains are fit subjects for taxation because they have greater ability to pay. While there is little doubt that the average chain store could afford higher tax levies than could the average independent unit, it does not follow that there is any real relationship between the number of stores in a chain and ability to pay. Chain-store-tax advocates assume, apparently, that all chains of the same numerical size have equal ability and are equally profitable. This is, of course, a denial of reality. If taxes are to be imposed in conformance with the "ability concept," then there should be some reasonable relationship between the amount of the tax and the degree of ability to pay. There is no such consistent relationship in the case of the chain-store taxes.

In this same vein it has been suggested that chain-store taxes can be justified in terms of the "benefit received principle." This is open to the same criticism leveled against the other concept. It is assumed here that all numerically similar chains experience the

same benefits when the state permits them to operate in chain form. Such is obviously not the case. The chain taxes bear little relation to the benefits presumably realized by the taxpaying entities.

One more argument is advanced in support of this revenue approach to the chain-store taxes. It is based on the contention that chain organizations escape certain of the other taxes levied by state governments, in particular the property taxes. The lower costs of inventory and the more rapid turnover in chain as contrasted with independent stores indicates that there is some considerable measure of truth to this argument. The real fault here lies not with the chains but with the state taxing systems, and in particular with the general property tax, which is quite unsatisfactory as a business tax. There appears to be little reason as to why the chains should be penalized for such deficiencies. The answer lies in the rejuvenation of antedated state taxing systems and not in throwing extra taxes upon business with little regard for consequences. If this were a reason and not an excuse for chain-store taxation it would be worth while suggesting that these taxes are scarcely adjusted to account for the degree to which the different chains do escape their share of state tax imposts. All chains are, however, treated on the assumption that those with many stores must certainly escape more of the taxes than those with few, regardless of the size of each store, the total inventory in stock, or the rates at which that inventory moves.

All of the foregoing suggests one major criticism which may be offered at this point. Taxes of the type illustrated by these chain-store levies constitute at best a very crude method of control. They make no allowances for real differentials between members of groups which are taxed and take little note of differences existing between such a group and others with which it competes. Such methods do not permit the niceties of refinement required of any good regulatory program. There is no flexibility to legislation of this type. It rests like a heavy club over all coming within its jurisdiction and is for that reason undesirable.

All of the criticisms directed at the state chain-store-taxing statutes apply with redoubled emphasis to the municipal levies of a similar nature. There can be no explanation for such statutes other than one based upon questions of political expediency. If there were any justification for such measures the state enactments would have adequately covered the field and there would be no room for municipal chain taxes of the same type. Further denunciation of municipal chain taxes arises from the excessively punitive nature of the burdens. Taxes are graduated so severely as to make chain operations almost impossible in taxing jurisdictions. Rates which bear no reasonable relation to profits or competitive conditions can be explained in terms only of the most selfish motivation, either through the presence of retail dealers on municipal legislative boards or the necessity of pleasing constituents who are retail dealers. There is little justification for such misuse of legislative powers and the immediate removal of municipal chain-taxing statutes is urgently recommended.

It may be said with regard to the proposed federal Patman chain-store-taxing bill that its effects would be quite different from those of the many state enactments. Where they tend at the most to discourage certain chain groups, the federal statute would eliminate all but the smaller chains. There would be absolutely no opportunity to shift the burden of such taxes to the consuming public. They would, of course, then have to be borne by the chains and, for the larger chains at least, this burden would be more than equal to chain profits. Such a measure would put an end to chain operations as they have been known in the past.

The Robinson-Patman Act has been in force for something more than two years. During that time it has been vigorously administered by the Federal Trade Commission.<sup>3</sup> During the first

<sup>3</sup> The Federal Trade Commission is not the only administering agency for this statute and no such implication is intended. The Department of Justice, the Interstate Commerce Commission, the Civil Aeronautics Commission, and the Secretary of Agriculture also have jurisdiction. The Federal Trade Commission does, however, have charge of the type of prosecution most relevant to the chain-store situation.

two years of enforcement the Commission investigated 515 alleged violations and completed 345 of them. Over one hundred of these cases arose in the food-products field, where the chain stores are strongest. The vigor of the enforcement of this statute lends added weight to the contention that chain taxes are unnecessary to prevent certain of the supposedly unfair practices of the chains. The Commission has been diligent in its effort to prevent unwarranted quantity-discount practices from continuing.

Although the Miller-Tydings Act had been in force less than one year, by June 30, 1938, the Federal Trade Commission had issued during that time five cease-and-desist orders and one complaint under the statute. This suggests that the federal resale-price-maintenance legislation when coupled with similar state enactments will be sufficiently effective in controlling loss-leader practices of the chain stores and that no taxing legislation may be justified on such grounds.

One final point remains to be treated. It has been suggested that these chain-store taxes give the co-operative chains an appreciable competitive advantage over their corporate rivals. Would it not, the question is asked, be desirable to impose similar levies upon the co-operatives in order to equalize the competitive position? In support of this contention it is argued that the voluntary groups have adopted all the techniques of chain-store operation, save only centralized control and ownership.

While these claims are unquestionably true, they do not appear to constitute a sufficiently strong argument to justify the extension of undesirable tax levies to a group which until the present has remained outside this punitive orb. It is impossible to offset the ills which confront a few by extending them to all. This study is not interested in pleading the case of any particular group of retailers. It is, however, concerned with the impact of various regulatory programs upon the well-being of the general public. The chain-store taxes are being condemned, not because they are chain-store taxes, but simply because they appear detrimental to general welfare. To argue that they should be extended to still

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other groups is to ignore the public interest in regulatory movements.

While it is, in all probability, true that these taxes do place the corporate chains in a much less favorable competitive position than was the case in the past, the solution does not lie in impeding the progress of other groups. The more logical course lies in the repeal of the corporate-chain taxes. Unfortunately, history shows that too often legislators are not logical in such matters. Nevertheless, repealed or unrepealed these taxes should not be extended to other groups.

Final recommendations follow.

#### CONCLUSIONS

It is recommended that all chain-store-taxing statutes of whatever type be repealed at the earliest possible moment.

This recommendation rests on the following points:

1. There is no need for such legislation, particularly since other federal and state measures control the more undesirable of the corporate-chain activities.
2. These statutes taxing the chains tend to accomplish almost none of their stated purposes, although they do come close to accomplishing some that are most undesirable and lead to certain results which are quite the opposite of those intended.
3. The statutes bear no reasonable relation to the nature of the subject matter of such legislation.
4. The statutes constitute a threat against general welfare in themselves.
5. They tend to encourage rather than discourage those elements in chain operation which are least acceptable.
6. There is no indication that society will be benefited by such legislation, and there are several indications that an opposite result will accrue.
7. The Indiana type of statute penalizes most severely the chains least in need of control, the smaller local and sectional groups.
8. None of the statutes, Louisiana type or Indiana, are based

upon any valid measure of size, but mistakenly assume that store numbers bear some relation to the issue.

9. The statutes are enacted to promote the interests of inefficient entities and demote the interests of more efficient groups.

10. There are some, although admittedly limited, possibilities that a part of the burden of these taxes will be shifted—forward to consumers and backward to producers, manufacturers, and middlemen—a condition undesirable from the standpoint of the general welfare.









